



# China-EU Leadership in Globalisation: Ambition and capacity

Weinian Hu and Jacques Pelkmans

## Summary

This CEPS Policy Insight attempts to offer a first verification of whether China and the EU are ready to exercise leadership in global trade and investment, not only in words but also in deeds that would underpin credibility for the world trading and investor community. A distinction is drawn between the ambition to exercise such leadership and the effective capacity to do so. The EU's capacity to lead is not at issue, but, as is shown, it does face a few difficulties. The paper analyses China's effective leadership capacity based on aspects of its energetic FTA strategy, investment protection agreements, the progress of its domestic market-oriented reforms (required for economic openness) and its record in negotiating the WTO plurilaterals. Some reflections on a possible joint leadership of the EU and China are offered in the conclusion.

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Weinian Hu and Jacques Pelkmans

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## 1. The idea of joint leadership, an introduction

Responsible globalisation policies require firm adherence to WTO principles, as well as mutual trust in the G-20 and beyond that trading partners further open their economies rather than revert to sneaky protectionism. Globalisation also ought to be legitimate in that domestic policies ensure that temporary losers do not incur significant risks and income losses when adjusting to new specialisations. In turn, this combination of international commitment and domestic assurances of reasonably smooth adjustment should be based on a strategic consensus amongst as many trading partners as possible, forged and maintained through leadership by the largest ones. In the G-20, there are three trade giants: the EU, China and the US, roughly equal in economic size. In the past, the US and the EU exercised a kind of joint leadership (a ‘bigemony’),<sup>1</sup> but those days are long gone. Today, of the three trade giants, China and the EU loudly advocate multilateralism and WTO-compatible free trade areas, whereas the new US administration is pursuing an ‘America First’ approach, blending the achieved openness with intended bilateral ‘corrections’, threats of punitive tariffs, and searches for currency manipulation whilst casting doubt on specific aspects of WTO rules or adjudication.

In both China and the EU, the inference is that leadership is more necessary than ever and that they have to be proactive in reinvigorating current strategies supporting responsible globalisation (Hu & Pelkmans, 2017). Indeed, the two trade giants would seem to be destined to exercise leadership together, given they share a crucial common interest and that not even a large economy can effectively lead alone. Even when the two decide to closely work together, they will still have to build wider coalitions in many ways. However, for leadership in trade and investment to be effective in stimulating cross-border economic intercourse, it has to be credible and enduring.

The present CEPS Policy Insight attempts to offer a first verification of whether China and the EU are ready to exercise leadership in global trade and investment, not only in words but also in deeds which underpin credibility for the world trading and investor community. We distinguish the ambition to exercise such leadership from the effective capacity to do so. Section 2 summarises a range of trade policy initiatives undertaken recently by China, which strongly suggest an emerging ambition to assume leadership in various forms of international economic cooperation. These include the APEC-wide free trade area, also known as the Free Trade Area of the Asia-Pacific (FTAAP), initiated by APEC economies in 2006 while China pushed for a road map to be endorsed by APEC leaders at the 2014 APEC Beijing Summit; the pro-globalisation speech by President Xi Jinping in Davos in January 2017; and the Chinese Ministry

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<sup>1</sup> See e.g. J. Pelkmans (1986), “The bickering bigemony: GATT as an instrument of Atlantic trade policy”, in L. Tsoukalis (ed.), *Europe, America and the World Economy*, Oxford: Basil Blackwell.

of Foreign Affairs April 2017 publication of “China’s Economic Diplomacy Entered the New Era”. Although not a pure trade initiative, one might add the 2013 Belt and Road Initiative (also known as “One Belt, One Road”, or OBOR) that is gradually taking shape, which is a long-term vision of Eurasian infrastructure and its financing (by the Asian Infrastructure Investment Bank), as well as the customs, transport and trade policy consequences of wishing to lower trading costs significantly throughout the vast OBOR territory. We add a short survey of China’s active FTA strategy and the status quo with respect to the bilateral investment treaties (BITs) it has concluded or is negotiating. We nonetheless allocate this part to Section 5.1, so we can examine it in light of China’s leadership capacity on domestic, regional and plurilateral fronts. Section 3 summarises EU trade and investment strategy, recently even more articulated in response to Trumpism in US trade policy. The EU’s ambition to exercise leadership in trade and investment originated in the GATT Dillon and Kennedy Rounds, was pursued via the so-called ‘Quad’ (EU, US, Japan and Canada), and continues today in loose, larger groups including the BRICS. The EU’s capacity to lead is not at issue, but, as will be shown, it faces a few difficulties. Section 4 zooms in on bilateral EU-China trade and investment relations, asking the question whether and how the demand for leadership is expressed in practical bilateral economic relations at this stage. China and the EU engage in many dialogues and common projects related to trade. The main frictions, though reasonably ‘contained’, concern trade defence instruments, e.g. for steel, and the methodology of determining the dumping or subsidy margin. Prominent amongst the far-sighted bilateral options is President Xi’s spring 2014 suggestion to explore a free trade area (FTA) between China and the EU. Another critical initiative consists in the ongoing negotiations on the Comprehensive Agreement on Investment (CAI). With respect to these two concrete and highly significant possibilities, we will perform a reality check to help the reader assess whether and to what extent the idea of leadership, even joint leadership, is likely to be deemed credible by traders, manufacturers, global value chains and investors. Does China in particular possess enough capacity to exercise leadership by example through these major initiatives? Section 5 continues the analysis of China’s effective leadership capacity by considering China’s dynamic FTA strategy, its investment protection agreements, and its record on both domestic market-oriented reforms (required for economic openness) and negotiating WTO plurilaterals. Section 6 concludes with some reflections on possible EU-China joint leadership.

## 2. China: A new entrepreneur in trade policy initiatives

### 2.1 Trade initiatives and domestic market reforms

In China, the profound and broad market-oriented reforms announced at the Third Plenum of the Party in November 2013<sup>2</sup> are bound to interact positively with initiatives to open up the economy. This is because a host of domestic restrictions in some goods and many services markets, as well as the privileged position of many state-owned enterprises (SOEs), imply, in

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<sup>2</sup> At the Third Plenum, the market’s decisive role in allocating resources was acknowledged. Note, at the same time, President Xi explained that a proper relationship between the market and government remains at the core of China’s economic reform. See [http://news.xinhuanet.com/english/china/2013-11/15/c\\_132891949.htm](http://news.xinhuanet.com/english/china/2013-11/15/c_132891949.htm).

most instances, restrictions to market access (for trade and investment) or even bans on doing business vis-à-vis EU (or foreign) businesses. On the other hand, some industrial upgrades in technology and higher value-added sectors, which are included in these reforms, might introduce or accentuate market distortions that disadvantage foreign businesses or effectively shut out foreign partners from new opportunities despite their potentially powerful competitive position. In addition, the incredible speed at which China is becoming an upper-middle-income country has resulted in many unattended domestic legacies (whether institutional or regulatory) of the old planning system and practices, which – more often than not – ‘throttle’ or distort markets, hindering domestic and foreign business alike and sometimes maintaining biases against foreign business. In short, given the rather fundamental reform intentions of China’s government and the eagerness to thrive on new, higher value-added business and economic growth models, the 2013 decisions of domestic “comprehensive reform and opening up”, in the words of President Xi, and China’s recent strategic trade and investment activism, are profoundly interconnected. The emergence of US protectionist threats and the ‘America First’ stance are not the fundamental drivers behind China’s new entrepreneurialism in trade, though they undoubtedly generate urgency and a greater will to refine strategy. Chinese ambition in trade and investment has become truly entrepreneurial. We shall discuss four significant strands of China’s new trade strategy.

## 2.2 Towards an all-APEC FTA?

First, when chairing APEC in 2014, China insisted that APEC should strive for an FTAAP. This initiative is not yet fully elaborated, because a collective strategic study on its realisation, which according to the Beijing Roadmap was expected by end-2016, has yet to be published. To best understand the FTAAP and the debate in APEC, it should be remembered that China was not part of the Trans-Pacific Partnership (TPP) as concluded before Trump took office; it was and is a member of the Regional Comprehensive Economic Partnership (RCEP) – initiated by ASEAN plus the six countries in the regular East Asia summits – which is an attempt to reduce trading costs of the spaghetti bowl of intra-East Asia FTAs, with its many inconsistent and complex origin rules. The upshot was a split among APEC members: the FTAAP was untimely, unsuitable or both.

The basic idea for an FTAAP is found in the “Beijing Roadmap for APEC’s Contribution to the Realization of the FTAAP”, which was annexed to the 22nd APEC Economic Leaders’ Declaration (Beijing, 2014). Common views shared by APEC leaders are that initiatives such as the FTAAP, as a major instrument to further APEC’s regional economic integration agenda, should be pursued on the basis of supporting and complementing the multilateral trading system. It should be comprehensive, high quality and incorporate and address ‘next generation’ trade and investment issues. It is best pursued by building on current regional architectures, such as the TPP and RCEP, and developing regional architectures, including possible pathways to the FTAAP. In accordance with the Beijing Roadmap, APEC members committed to “at the border” trade liberalisation and facilitation, improving the “behind the border” business environment,

and enhancing regional connectivity “across the border”, including areas such as investment, services, e-commerce and rules of origin.<sup>3</sup>

The FTAAP faces two major problems. One is the elaboration of an all-APEC FTA blueprint and roadmap – not an easy task given the considerable disparities in views and current trade policies. This is presumably the principal reason why the roadmap took more than three years to draft. The other problem is new: the all-APEC FTA is unlikely to be welcomed by the Trump administration, which means China will have to carefully consider whether – at this stage – it might not be wiser to find an accommodation with the TPP-11 group. This alternative would be consistent with the spirit of the intended Chinese domestic reforms and be widely understood as a manifestation of new trade leadership by China. For example, the chapter on SOEs of the TPP establishes comprehensive standards on SOE management (although there are exceptions for sub-central SOEs, and thresholds apply). Why not emphasise this chapter’s content as a means of exerting “external pressure” to lift the impediments that may have caused delays in implementing SOE reform pledges? But pride may have prevented China from establishing a partnership with the TPP-11 because the TPP initiative was widely regarded by Chinese policy-makers and scholars as an anti-China initiative. The recent TPP-11 meeting in Chile was attended by China, but next to nothing has been reported on it.

### 2.3 President Xi’s pro-globalisation speech in Davos

President Xi surprised the world with his pro-globalisation speech in Davos in January 2017. The surprise is not so much that China has a great stake in globalisation – this is of course well-known and has been recognised many times by Chinese leaders. What amazed many observers was the strident plea against anti-globalisation movements and populist politics (“many of the problems troubling the world are not caused by globalisation”). The constructive and balanced speech emphasised a global “balanced, equitable and inclusive development model”, “fair and equitable governance”, and a “well-coordinated and interconnected approach to develop a model of open and win-win cooperation”, stressing that “no one will emerge as a winner in a trade war”. There was also firm language on Chinese reforms, such as: “China is committed to a fundamental policy of opening up”; “China will boost market vitality to add new impetus to growth”; “intensify reform efforts in priority areas”; “foster an enabling and orderly environment for investment”. President Xi confirmed that China “will advance the building” of the APEC free trade area.

### 2.4 China’s strategy of economic diplomacy

In “China’s Economic Diplomacy Entered the New Era”, Director-General Zhang Jun (of China’s Ministry of Foreign Affairs) published a clear, though generally worded, five-point strategy for China’s economic diplomacy (Zhang, 2017). For example, Point I, “Guiding World Economy”, emphasises openness and win-win cooperation, with China acting not only as an anchor but also as an “engine and tractor”. Zhang is explicit regarding China’s pursuit, even against intra-

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<sup>3</sup> See <http://apec.org/Home/Groups/Other-Groups/APEC-Study-Centres-Consortium>.

APEC lack of enthusiasm, of the FTAAP. Point II, “Championing Global Development”, citing China’s initiative at the 2016 G-20 Hangzhou Summit, advocates a “distinctly pro-development agenda and outcomes”, and calls (as Xi did in Davos) on all signatories of the Paris Climate Agreement to stick to their commitments, thus reflecting China’s “strong sense of responsibility”. Point III, “Improving the Model of Economic Governance”, calls for striving towards a “more equitable, reasonable, reliable and efficient” system, based on the idea that BRICS and emerging ‘BRICS’ ‘have been gradually taking up the central place on the world stage’. At the Hangzhou summit, “China vigorously encouraged the G-20 to remain relevant” and to transform itself “from a crisis-response mechanism to a long-term governance mechanism”. Point IV, “Supporting National Development Strategies”, addresses international financial institutional reform and claims China achieved “breakthroughs” on increasing the representation and voice of emerging markets and developing countries. “During China’s G-20 presidency...the long-delayed IMF quota reform plan was followed through, the RMB was included in the SDR currency basket...the International Financial Architecture Working Group...was relaunched”. Chinese initiative or close collaboration with China, the article reads, established the New Development Bank (“the first international institution independently founded by developing countries”) and the Asian Infrastructure Investment Bank (AIIB) related to Belt and Road proposals, “spearheading the reform and improvement of the global economic governance system”.

In addition, China is adamant in claiming to support both its partners’ national development strategies and international economic cooperation, that is, “mutually beneficial cooperation to help advance economic transformation at home”. The Belt and Road Initiative is presented as strengthening “complementarity between development strategies of China and relevant economies”. Finally, Zhang proudly boasts of “showcasing China’s confidence” in Point V, “Sharing of China’s Development Philosophy”.

## 2.5 Belt and Road Initiative and China’s trade policy

The Belt and Road Initiative (OBOR), intended to better connect China with Central Asia and Europe via infrastructural investments of a mind-boggling magnitude, is an entirely novel set of projects. But plans are at best sketchy. This is due to the enormity of the overall idea and the immense amount of required public, private and mixed funding. However, it is also due to the nature of international cooperation between the many countries that will have to shape and develop, step by step, the commitments, infrastructure hardware and numerous treaties and cooperative agreements to make OBOR a success. The establishment of the AIIB, including cooperative links with the EBRD, the EIB and 57 countries as founding members (including most EU, ASEAN and South Asian countries, though excluding the US and Japan), can be hailed as an early example of Chinese leadership. At the just concluded Belt and Road Forum (14-15 May in Beijing), China announced plans to establish an FTA network of 20 countries involved and located in OBOR territory. Through OBOR, China aims to promote “trade connectivity” with 60 countries and international organisations, based on the principle of “common discussion, common building and common sharing” and by seeking consensus on joint action (MOFCOM,

2017b). China has already implemented FTAs with 12 countries in OBOR territory (MOFCOM, 2017a), including the China-Georgia FTA signed during the forum. Based on available information, the focus of this FTA is bilateral tariff reduction and elimination, with both sides committing to greater openness in service sectors.<sup>4</sup> It has also been announced that China and Mongolia will start a joint feasibility study in order to launch FTA negotiations.

### 3. EU trade and investment strategy: Ambition and capacity

The EU has always been a strong supporter of multilateralism, via the WTO. It has been in the forefront of all the GATT (and now WTO) Rounds, often with initiative papers and proposals. Following the Uruguay Round, it has attempted time and again to honour the development dimension of the Doha Round. For example, though not to much avail, the EU proposed four (so-called ‘Singapore’) issues to be addressed by the WTO: government procurement transparency, trade facilitation (customs issues), trade and investment, and trade and competition; stimulated the Multilateral Agreement on Investment (MAI) negotiations in the OECD (which failed in 1998, as they were seen as too ambitious and the requirements not lenient enough for developing countries, although most developing countries subsequently concluded numerous BITs); and systematically supported a range of other initiatives, from the International Trade Centre, which helped developing countries in trade matters, to the Trade Facilitation Agreement concluded in Nairobi. It should also be noted that the EU self-imposed a moratorium on FTAs from 1999 to 2006 in order to increase incentive to accelerate the Doha Round. Finally, the EU has been an active supporter of China’s entry into the WTO, beginning long before the US was convinced that the terms of entry were right. In other words, the EU has shown for decades both ambition and capacity for leadership in trade and investment.

So far, the EU has a network of 38 active bilateral and regional trade agreements covering 67 partners in the rest of Europe, the Mediterranean and the rest of the world from Azerbaijan to Cameroon, Canada to Papua New Guinea, Fiji to South Korea. Although the core of these agreements are FTAs, 13 are different variants such as association, customs union, partnership and cooperation, stabilisation and association, interim, cooperation, interim economic partnership, economic partnership and cooperation, stepping stone economic partnership. The objectives of these agreements – depending on the specific kind as well as the levels of ambition – include removing or cutting customs duties on goods, scrapping any tariff quotas,

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<sup>4</sup> The China – Georgia FTA seems to be another example of China’s conventional FTA model, which focuses on tariff reduction and elimination. The FTA has 17 chapters, including goods, services, rules of origin, customs procedures and trade facilitation, and intellectual property rights protection. Based on the available information released by MOFCOM, it is noted that, in the service chapter, both sides pledged to a ‘deep’ opening up, while Georgia made concessions and met China’s primary requests in the areas of financial and transportation services, movement of people and Chinese traditional medicine. China made concessions in tourism, shipping and legal services. See [http://fta.mofcom.gov.cn/article/zhengwugk/201705/34957\\_1.html](http://fta.mofcom.gov.cn/article/zhengwugk/201705/34957_1.html) (Chinese).



allowing EU businesses to provide services and bid for public contracts, cutting red tape in order to facilitate exports, etc.<sup>5</sup>

In the face of anti-globalisation sentiment, the EU reaffirmed its open market strategy and commitment to free trade. On 8 March in Singapore, EU Commissioner for Trade Cecilia Malmström stated that “31 million jobs in Europe depend on exports beyond its borders...and free trade deals expand those opportunities further” (Malmström, 2017). In response to Trumpism, the EU unveiled an even more ambitious trade agenda that will “double down [o]n advancing our own trade talks with partners around the world, including the countries of the TPP”. The prerequisite (following from the EU treaty) for becoming a preferred trade partner of the EU is shared values, such as human rights, the rule of law, and environmental protection, as well as signing core ILO Conventions.

An investment strategy at EU level is new (since the 2009 Lisbon Treaty). What emerges as its investment strategy may best be illustrated by the scope of the EU-China CAI negotiations, which encompasses market access opportunities without discrimination, high and balanced protection for investors and investments, and a better regulatory environment relating to transparency, licensing and authorisation procedures. On the EU side, the openness of the single market to foreign direct investment (FDI) is unconditional, except for some local (e.g. environment) conditions. But in the case of China, where ‘reciprocity’ in market access for EU investors is lacking in a number of sectors, an EU desire to at least screen FDI when hi-tech or critical infrastructure is concerned, especially when SOEs target EU companies, is building. Some EU member states are seen as “flirting with protectionism” (Michalopoulos, 2017b) when they want to screen foreign takeovers, usually on grounds of national (economic) security which can be stretched rather wide. China-specific concerns about security and unfair competition relate to state interference in market forces and to sensitivities that the lines between the public and the private sectors are blurred (Grieger, 2017). This debate on whether or not Chinese FDI should be subject to screening has been going on ever since the financial crisis, but the unease within the EU has recently increased. The Commission might perhaps consider foreign investment review mechanisms to ensure EU countries do not unwittingly lose their industrial capabilities and competitive advantages (Heath, 2017). So far, there is no FDI screening or approval regime at EU level; the Commission has always followed its ambitious agenda of attracting investment and creating jobs. The general view is that, because Chinese investors in Europe typically do not limit themselves to a short-term outlook and focus on long-term strategic investment (Jungbluth, 2016), member states need to keep an open mind and shelve protectionism.

The EU’s capacity for leadership has long been established. However, this is not to be interpreted as a problem-free. Presumably, this is true for all countries aspiring to (help) lead trade and investment in the world economy. There are three aspects where the EU’s capacity is possibly affected negatively. First, the EU has gone unusually far in offering access to a free

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<sup>5</sup> See [http://ec.europa.eu/trade/policy/countries-and-regions/agreements/index\\_en.htm#\\_europe](http://ec.europa.eu/trade/policy/countries-and-regions/agreements/index_en.htm#_europe).

and uniformly regulated single market in trade and investment talks. But in some areas (at member state level) protection lingers, which does not accord well with leadership by example. Thus, in the EU-Canada Comprehensive Economic and Trade Agreement (CETA), very lengthy annexes have been agreed to for services and FDI, based on restrictions retain by EU member states. It would seem that the economic meaning of these restrictions is minor, if only because companies from the partner country (Canada) may relocate to another member state, thereby reducing or avoiding such restrictions. Nevertheless, retaining hundreds of pages of restrictions in annexes is not what leadership is about. Second, EU trade treaties are negotiated by the European Commission, in accordance with a mandate from the Council, i.e. member states, and ratification requires the assent of the European Parliament. However, with modern so-called ‘deep and comprehensive agreements’, a treaty often comprises issues which fall under national, not EU, competences. Given the significant regulatory content of such treaties, the sensitivity of (some) political parties to provisions dealing with ‘behind the border’ issues that are often within the purview of national powers has greatly increased. This can potentially undermine the EU’s capacity to exercise leadership if and when just one (!) member state decides not to ratify a so-called ‘mixed’ agreement, i.e. an agreement with articles under EU and national competences. A 16 May CJEU ruling on the Singapore/EU FTA considerably mitigated this risk of reduced credibility of trade partners, in specifying that almost all areas in doubt, e.g. transport modes, investment, etc., fall under EU competences for trade agreements. In practice, this means that trade treaties can be credibly negotiated except for a few genuinely minor issues, e.g. portfolio investment (but not FDI), which can be ‘parked’ in a separate mini-treaty that would be subject to two-level ratification.

Thirdly, there is also a question of bringing non-trade issues – value-based questions notably on human rights, sustainable development, climate change, basic labour standards, etc. – into trade agreements. When the EU negotiates a trade agreement with 1) a “like-minded” partner, such non-trade issues may not cause any arguments and rather be dealt with in a routine manner; 2) with an economically weaker partner, the EU may very well use its leverage to incorporate non-trade issue clauses in the agreement (for example, the EU-Vietnam PCA), although it is not clear how the EU would act in case of a violation; 3) with a partner like China, which has considerable strengths and influence and is governed by a different political philosophy, the EU may struggle to use any economic leverage effectively. Recall that nearly 10 years ago the EU and China had to abandon partnership and cooperation agreement (PCA) negotiations. After some delay, a new start was made with CAI negotiations, leaving non-trade issues, e.g. human rights and labour questions, to bilateral dialogues for exchanging views and cooperation. Therefore, the EU’s capacity for globalisation leadership might be compromised in certain instances when mixing non-trade issues with trade issues in a trade agreement, which is nonetheless a principle laid down by the Lisbon Treaty and that the EU must follow.

#### 4. Forging closer bilateral trade and investment relations

PCA negotiations were abandoned because of China's firm resistance to mixing non-trade issues in trade negotiations. Thus trade issues and non-trade issues were separated, some of the former included in the CAI talks, the latter pursued by means of a wide-ranging cooperation programme encompassing over 60 bilateral dialogues on, e.g. climate change, urbanisation, agro-food safety, (consumer) product safety, intellectual property rights protection and human rights protection. The CAI stand-alone negotiation is a result of the PCA failure, i.e. separate investment negotiations without non-trade issues.

Somehow, China expressed its wish to follow another route, with a small delay. Barely 3 months after the first round of CAI negotiations in January 2014 in Beijing, China's President Xi (in his speeches at the College of Europe and in Brussels) called for exploring an EU-China FTA. The EU responded much later that the EU would be interested in a FTA with China, on conditions of a satisfactory outcome of the CAI negotiations and the country's leadership in multilateral trade negotiations.

A (deep and comprehensive) FTA will certainly benefit both the EU and China, as our extensive analysis demonstrates. Pelkmans et al. (2016) find that the extra GDP for China (in percentages) will be 2.5 greater than the EU's gain. Note that the model simulation is necessarily a considerable underestimate, because the CAI's economic impact – an EU prerequisite for a 'deep and comprehensive' FTA – and several other aspects, e.g. innovation, are not incorporated.<sup>6</sup> The trade effects of the FTA are quite powerful, too, with more than a doubling of EU exports and a 60% increase in the already vast amount of Chinese exports (of goods mainly) to the EU. There will be real wage gains among all three skill levels of workers, i.e. low-skilled, medium-skilled and high-skilled workers; these wage gains equally extend to Chinese workers. As to changes in EU and Chinese trade patterns, EU exports to China would increase by 110% (an ambitious scenario) whereas China's exports to the EU would increase by between 56.9% (also ambitious), with a greater increase for China in total exports than for the EU (Pelkmans et al., 2016: 272-305).

Greater openness beyond a bilateral EU/China FTA would bring further gains and should also underpin China's ambition of trade and investment within the context of the Belt and Road Initiative, and where many European countries are involved via the AIIB. As noted, China just announced the objective of consolidating an FTA network of 20 countries in OBOR territory. But before that is achieved, China may need to elevate itself to a higher degree of market openness to foreign investors, on top of the WTO commitments it has fulfilled in the last 15 years. Leadership in the world trade and investment cannot but imply being ahead of the WTO, especially where it has been stuck in the past, as is the case with investment. There is no WTO-led regime for investment, which was rejected as a taboo Singapore issue, except for the Agreement on Trade-related Investment Measures (TRIMs), covering trade in goods only and

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<sup>6</sup> For extensive treatment of model shortcomings that cause the estimates to be much too low, see Pelkmans et al. (2016), pp. 272-305.

merely addressing the worst restrictions of investment in this regard, i.e. performance requirements. Together with the scope of CAI negotiations, as mentioned above, it is understood that China needs to negotiate to open its service sector. Additionally, given the principle of reciprocity, the objectives of concluding an EU-China CAI are to agree on pre-establishment national treatment and provide post-establishment non-discriminatory measures. With respect to investment/investor protection for the purpose of increasing certainty and predictability, China might consider adopting the Investment Court System, an EU proposal for a multilateral system accepted in the meantime by Vietnam and Canada in their PCA and FTA with the EU, respectively. Presently, under China's bilateral investment treaties, disputes are settled through diplomatic channels, domestic litigation or, when disputes arise between the hosting contracting party and the investor, arbitral tribunal. Investor-state dispute settlement (ISDS) is usually incorporated in China's BITs. Improving its regulatory environment has much to do with the legacy problems in China, as a result of a planned, top-down regulated economy following the feudalism that had lasted for more than 3,000 years. This question will be addressed in detail in subsection 5.1 on China's capacity to assume global leadership.

One needs to bear in mind that concluding an EU-China CAI is only half of what could be accomplished to fulfil the enormous trade potential between the two sides. A bilateral FTA should be the next step, and the ambition is to design it in a "deep and comprehensive" manner (the approach adopted by the EU in its trade negotiations). It seems China is moving into this direction, as one hears similar language (in a literal sense) from the Ministry of Commerce for example about the China-Japan-Korea trilateral FTA negotiations. Being "deep and comprehensive" is to specify and complement the principles and rules that the WTO lays down, a state of depth and scope also known as "WTO plus". So far, the FTAs that China concluded may be described as "shallow", as their emphasis is usually on tariff reduction or elimination, other duties, e.g. anti-dumping duties, tariff-rate quotas (often employed for agro-goods) and some customs issues. The latest China-Georgia FTA is an example. Nonetheless, the tendency observed is that these FTAs are considered 'living' agreements, which means there is a fixed schedule and a precise list of subjects envisioned for future negotiations. In general, opening up the service sector is often on the list.

## 5. Scrutinising China's capacity to exercise trade 'leadership'?

### 5.1 China's FTA and BIT activism

In the words of the Chinese Ministry of Commerce, China deems "FTAs as a new platform to further opening up to the outside and speeding up domestic reforms, an effective approach to integrate into global economy and strengthen economic cooperation with other economies, as well as particularly an important supplement to the multilateral trading system."<sup>7</sup>

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<sup>7</sup> See <http://fta.mofcom.gov.cn/english/index.shtml>.

Table 1. The state of play of China's FTAs

FTA	Concluded	Under negotiation	Under consideration (joint feasibility studies)
China	Australia, Korea, Switzerland, Iceland, Costa Rica, Peru, Singapore, New Zealand, Chile, Pakistan, ASEAN, Hong Kong (closer economic and partnership arrangement), Macau (closer economic and partnership arrangement), Georgia (concluded 15 May 2017 <sup>8</sup> )	ASEAN (upgrading), RCEP, GCC (Gulf Cooperation Council), China-Japan-Korea trilateral, Sri Lanka, Pakistan, Maldives, Israel, Norway, Eurasia Economic Union	India (regional trade arrangement), Colombia, Moldova, Fiji, Nepal, Mauritius, Mongolia (announced 15 May 2017)
	Asia-Pacific Trade Agreement (preferential trade agreement)		Asia-Pacific FTA

The queue of priorities in relation to China's FTA partners is based on China's four-dimensional FTA strategy (Hu & Pelkmans, 2017), which is: great powers as the key, neighbouring countries as the priority, developing countries as the basis, and multilateralism as the important venue. Per Table 1, China's FTAs with developing countries are either signed or under negotiation, so is the case vis-à-vis neighbouring countries and additionally a number of joint FTA feasibility studies are undertaking which means an FTA is under consideration.<sup>9</sup> At the same time, China is also a member of regional or partial FTAs (the latter are allowed in the WTO only for developing countries), such as the Asia-Pacific Trade Agreement (APTA). In APTA, China is negotiating three framework agreements on trade facilitation, trade in services, and investments.<sup>10</sup> Moreover, China is negotiating the China-Japan-Korea trilateral FTA, the RCEP, the China-Eurasian Economic Union Trade and Economic Cooperation Agreement as well as preparing FTAAP proposals, as noted before. This state of play suggests that China is now ready to progress to negotiating FTAs with leading trading partners who are 'great powers' in order to unlock greater trade potential.

<sup>8</sup> See [http://fta.mofcom.gov.cn/article/zhengwugk/201705/34957\\_1.html](http://fta.mofcom.gov.cn/article/zhengwugk/201705/34957_1.html) (Chinese).

<sup>9</sup> Note that presently China is conducting FTA upgrading negotiations with New Zealand, Peru, Chile and Switzerland; holding exploratory discussion with Canada on an FTA; and signed a declaration of intent with Australia on the "deliberation of related contents of the China-Australia FTA" in March 2017 (<http://fta.mofcom.gov.cn/list/enrelease/1/encateinfo.html>).

<sup>10</sup> APTA has seven members: Bangladesh, China, India, South Korea, Laos, Sri Lanka and Mongolia. South Korea is not regarded as a developing country anymore and cannot, therefore, conclude partial preferential agreements on tariffs.

China has long been active in negotiating investment protection agreements, or BITs. As of today, China has concluded 145 BITs,<sup>11</sup> and is negotiating a CAI with the EU<sup>12</sup> and a BIT with the US. After no fewer than 22 rounds, the predicament of the China-US BIT negotiations remains unknown since the Trump Administration took office. There is little transparency on how far negotiators had come. It is informally suggested that the two sides were at an advanced stage of text negotiation on the BIT, while at the same time observing that the exchange of negative lists by the two parties was ‘challenging’. Apparently, one major sticking point is ‘national treatment’ and its exceptions.

In relation to the EU-China CAI negotiations, the latest news was shared at a 15 March press conference concluding the “Two Sessions” (the National People’s Congress and the National Committee of the Chinese People’s Political Consultative Conference). Premier Li Keqiang revealed that China had called for accelerating CAI negotiations, and was awaiting a positive response from the EU. According to the 18 May Ministry of Commerce press release regarding the 13th CAI negotiation round in Beijing, both sides “will speed up the work and strive to promote the negotiation to make positive progress.”<sup>13</sup> Note that Premier Li also said at the Two Sessions that, even in the absence of the CAI, China would continuously enhance market access for, and extend equal (‘national’) treatment to, EU businesses as if they were local Chinese enterprises. This would be very welcome news. After all, based on the 2016 OECD FDI Regulatory Restrictiveness Index, China is 60th most restrictive country (among 62 countries surveyed). Compared to the 2015 index, when China was the most restrictive of all, it moved two positions down, doing better only than the Philippines, Myanmar and Saudi Arabia.<sup>14</sup>

So far, we have shown that China has developed the *ambition* to exercise ‘leadership’ in trade and investment, in a spirit of responsible globalisation. We now ask the question whether China has demonstrated the *capacity* to practise credible leadership.

We do this by posing three questions: Has China largely overcome transition problems from its formerly planned economy? Is China capable of effectively implementing the fundamental pro-market reforms announced in late 2013? How has China performed in the four plurilaterals negotiated by groups of avant-garde trade partners in the WTO? If the answer to these three queries is ‘yes’, or at least positive, one can infer that an effective leadership capacity exists and could be exercised in close partnership with the EU.

China is a relative newcomer in modern global trade; it has managed well to implement principles and rules dictated by the WTO. But assuming leadership implies, in technical terms, electing higher standards, i.e. “WTO plus”, for pre-establishment market access, for example. Impediments seem to exist and could be due chiefly to legacy issues. Therefore, China is likely

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<sup>11</sup> See: <http://investmentpolicyhub.unctad.org/IIA/CountryBits/42>.

<sup>12</sup> In fact, the EU and China are also negotiating an agreement on (more) geographical indications.

<sup>13</sup> See <http://english.mofcom.gov.cn/article/newsrelease/significantnews/201705/20170502578131.shtml>.

<sup>14</sup> Myanmar and Saudi Arabia shared the second position in the most restrictive rankings. See <http://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX>.

to have to complete some ‘homework’ in order to progress to earn the credentials for assuming global leadership.

## 5.2 Existing legacy issues delay China’s reform agenda

The main legacy issues are found in the areas of technical barriers to trade (TBT), sanitary and phytosanitary (SPS), services, public procurement, intellectual property rights (IPR) protection, geographical indications, investment (market access, non-discriminatory treatment, etc.), SOEs and competition policy. For example, in terms of TBT as a legacy of a planned, top-down regulated economy, China does not have standardisation bodies like those in most other WTO member countries. These are private bodies creating market-driven standards, which can – at times – also be employed for regulation. There is even a fundamental problem of terminology (for example, what a ‘technical standard’ really is) not being in line with the TBT Agreement and annex applied by standardisation bodies worldwide. There is also fragmentation of the Chinese (not so) single market and a legacy of far too many institutions, ministries, agencies and others having some ill-defined regulatory or standardisation competence (which they are loathe to give up), with uncertainty and unproductive overlap as a result. The Chinese leadership therefore decided to begin a genuine overhaul of the system in 2015. However, the reform plans do not include the creation, in the market, of private, independent standards bodies such as CEN/CENELEC or more or less similar US bodies. In the service sector, some services markets in China are *de facto* closed to investors but also to cross-border trade. The country is far behind in services value added as a share of GDP, even compared to other BRICS, presumably due to its emergence from a planned economy (where services ‘did not matter’) and the initial emphasis on heavy industries and export-led growth via assembly. Effective transformation has to be based on internal political forces and lingering (but ‘former’) institutions, and this despite legacies, unlike the experience of Central European countries in transition, which used the EU, its central principles and market governance as an anchor and beacon. Amongst these legacies are the SOEs, which are prominent in services markets owing to regulations (and bans for others) and great market power, not to mention their privileged access to finance and high-level political support (directly from the Party). An FTA between the EU and China cannot possibly be imagined without an ambitious services chapter (in combination with drastic mode 3 (FDI) liberalisation). At the same time, Chinese reforms would be neither serious nor in the service of its new economic model if the services sector was not opened widely. China can kill two birds with one stone via bilateral (and perhaps also plurilateral) liberalisation of access to services markets. Box 1 presents in summary form a range of issues where legacies play a role.



*Box 1. Legacy issues and reform issues for China's trade openness***Public procurement**

Public procurement (Pelkmans et al., 2016: 343-351) is not in any of the FTAs China has concluded so far. China is currently negotiating its WTO GPA accession, and the process (begun in 2007) has served as motivation for China's institutional reform of its public procurement system. Extensive concessions have been made in the GPA offers (see below), but SOEs have not yet been offered as a covered entity.

What EU businesses insist on is that China offers more entities at more administrative levels and in more provincial territories with even more lowered thresholds. All these demands are in addition to the EU's insistence on establishing a more transparent and non-discriminatory institutional framework.

An FTA with China would be on a GPA-plus basis, if the EU has its way. Addressing the SOE question in earnest is a crucial interest of the EU. Therefore, it is indispensable for China to join the GPA first, as a stepping stone to negotiating public procurement in an EU-China FTA.

China is closed to foreign competitors that bid for public procurement contracts, except in cases of shortages of technology. Essentially, public procurement is not seen as a component of trade but a device for budgetary control and discipline and therefore a means to eliminate corruption and use public funds more effectively.

Based on its WTO Accession Protocol, China started negotiations to accede to the GPA in 2007. The concessions made by the six GPA offers were extensive for (i) widened coverage of both procuring entities and (ii) relevant goods, services and works, as well as (iii) lowered thresholds. Additionally, China opted for a three-year, instead of five-year, grace period to implement the GPA upon accession. Moreover, in China's sixth offer (December 2014), activities in the fields of drinking water, electricity, energy, transportation, telecommunications and postal services were offered for procurement coverage, which is symbolic since these sectors are typically SOE-dominated. As mentioned above, SOEs have not yet been offered as covered entities in China's GPA offers to date.

**IPR protection**

China's IPR policy/law is ambitious in providing protection that is in the country's best interest in achieving an innovative economy.

The only problem, and a major one on the Chinese side, is implementation, i.e. delays, inconsistency and enforcement. Counterfeiting is also a problem when two-thirds of all detected counterfeit goods on the EU borders are from China.

China achieved spectacular success in IPR legislation in three decades and yet IPR enforcement is still weak. Issues hampering EU-China bilateral trade include administrative enforcement, patent linkage, admissibility of supplementary data for pharmaceutical product patent applications, enforcement on trade secret theft and ownership of copyrights.

The depth and breadth of IPR protection measures are on the increase in China's FTAs in recent years. In 2015, the IPR chapters in the China-Korea and China-Australia FTAs provided in great detail the degree and scope of IPR protection, with a 'TRIPS+' (Trade-Related Aspects of Intellectual Property Rights) approach.

**Geographical indications (GIs)**

China ranks in the EU's top five destinations for GIs exports (agricultural products, foodstuffs, wines and spirits), is now the world's fourth-largest importer of food, and the food and grocery retail market is set to grow by 15% annually.



The EU and China are presently negotiating a ‘comprehensive’ agreement on GIs, which goes beyond China’s so-called ‘best endeavour’ type of commitments in its FTAs to date. In addition to strengthening cooperation in protection and supervision and combating counterfeiting, the agreement should pave the way for more European GI-protected goods to penetrate the Chinese market, and vice versa on a reciprocal basis, establishing a foundation for easier concluding of GI negotiations.

China, as a latecomer to GI protection, has a range of local products corresponding to the concept of GI, but only a few of them are known or protected globally. At the end of 2012, 10 Chinese food names received protected status in the EU as GI as a result of the EU-China Geographical Indications “10 plus 10” pilot project. Since then, there has been no application for the protection of extra Chinese GIs. GI protection in China is hindered by fragmented registration and protection systems, which are often embroiled in disputes among business interest groups.

Among China’s 14 FTAs, bilateral GI protection appears only in the FTAs with Peru, New Zealand, Australia and Switzerland, but the provisions are of ‘best endeavour’ type, without substantive commitment.

## Investment

The EU-China CAI negotiations began in September 2012. In January 2016, the two parties announced there would be a wide scope to CAI negotiations, which should improve market access opportunities for their investors and guarantee that they will not discriminate against their respective companies, as well as to provide for a high and balanced level of protection for investors and their investments. Key challenges of the (mainly Chinese) regulatory environment, relating to transparency, licensing and authorisation procedures, are also on the negotiating table.

The EU is determined to see a good outcome from the CAI negotiations, which would be a condition for an FTA. As for China, it pursues further ‘opening up’ based on its own agenda. This agenda is full of pro-market reforms, is in very general terms, has taken longer than expected and resulted in very little to show in actual practice for business. Therefore, when pressing ahead with its CAI demands, the EU ought to ask itself what effective leverage it has. Will integrating CAI into an FTA not be a more sensible and effective option or would it postpone by a few more years improved investment market access?

Investment obstacles in China are of two types. The first type consists of the overall Chinese investment strategy, based not so much on principles of free markets (with an exception here or there) but rather on categorising FDI in four classes: prohibited, restricted, allowed and encouraged. This regime is adapted over time so that it amounts to an industrial strategy or what are called ‘structural policies’ that fit into China’s five-year plans. Therefore, various access issues are found in the first three classes. The second type refers to ‘post-establishment’, when EU (and other foreign) investors experience an uneven playing field for doing business, i.e. a myriad of policy restrictions and forms of discrimination.

For the investment chapter under FTAs concluded by China, substantive provisions on market access are left for further negotiations post-FTA. Moreover, what China has agreed to offer in terms of market access (pre- and post-establishment) typically reduces the EU’s demands by half. For example, the ‘pre-establishment’ phase of investment is not covered under national treatment, while what is covered are “expansion, management, conduct, operation and sale or other disposition of investments in its territory”. “Performance requirements” comply with the Agreement on Trade-related Investment Measures (TRIMs), which are only applicable to trade in goods. In contrast, the EU wants cross-border “trade in services” as well as least-restrictive local services provisions in most services markets to be included as a priority in the FTA.

### State-owned enterprises (SOEs)

The EU is adamant that the SOE question be settled once and for all, for the good of China (a kind of “external pressure” China often says it welcomes and benefits from, such as in the case of WTO accession) and to achieve undistorted market-driven economic relations with WTO partners.

SOEs’ privileged access to finance and preferential policy is a major legacy problem in China. Despite significant, relentless reforms in the recent decades, SOEs are far from being treated in a non-preferential way and solely under commercial considerations (Art. XVII, GATT). They wield enormous market power in a series of large-scale industries and a range of service markets, and are protected by a battery of restrictions or outright bans.

Following the Third Plenum in 2013, China pledged to reform its SOEs, reducing the subsidies they have enjoyed and diluting state holdings. But it remains to be seen how China will implement all these measures within the set timeframe up to 2020.

The China-Korea FTA does not incorporate an SOE chapter, although the intense Korea-China economic intercourse is profoundly influenced by the restrictive business environment.

### Competition policy

The EU and China have worked together in this field for more than a decade and it is now beginning to show results, in particular with respect to merger control. The 2008 Anti-Monopoly Law (AML) covers monopolistic operations that have anti-competitive effects on the Chinese market (that is, operations within China as well as activities outside China that affect the domestic market). EU competition law serves as the main reference for the AML on restrictive business practices, abuse of dominant position (cf. Arts 101, 102, TFEU) and the EU Merger Regulation.

SOEs impede China’s implementation of an effective competition policy, since they do not seem to be subject to competition policy in accordance with Art. 7 of the AML. In the absence of specific implementing rules, this defeats the purpose of competition policy.

EU businesses complain that China’s competition policy (AML, in particular, with respect to mergers) principally targets foreign businesses. But after a careful reality check, this allegation appears to hold little truth. Other complaints focus on implementation practice (especially the merger and acquisition transaction review), procedural rules, transparency, and enforcement discrepancies in different localities with regard to price-related investigations due to local interest and protectionism.

So far, China’s competition chapters in its FTAs feature provisions on cooperation that are principles-based, but the EU prefers to negotiate hard commitments. It favours detailed provisions, not just soft-law approaches to substance, for example, on ‘specific subsidies’ which are permissible depending on proper justification, whereas blanket and unlimited subsidies should be prohibited. Such commitments would have a very significant effect on China’s SOEs.

## 5.3 Effective and credible domestic reforms

China’s present domestic reform agenda is governed by the decisions delivered at the Third Plenum (November 2013) and on the 13th five-year plan (November 2015). In essence, and in relation to trade, the market is to be given a decisive role in allocating resources. This might be translated as implying considerable SOE reforms: letting market forces govern their commercial

decisions, withdrawing SOEs' convenient ready access to public finance with preferential rates and terms, and government policy, all of which result in overcapacity, staggeringly bad loans, market distortion, an un-level playing field given the restrictions applied to principles in international trade, such as national treatment, most-favoured-nation treatment and transparency. Specifically, ambitious SOE reforms holds the key to advancing China's position in multilateral trade negotiations, as well as to reaping more ambitious outcomes from trade agreements on bilateral and regional fronts. However, the general sentiment among foreign businesses in China is not so encouraging; patience seems to be waning.<sup>15</sup> These businesses noted that many reform measures tabled at the Third Plenum have been left unattended, or at best half addressed. In some areas, it is alleged that there were even worrying signs of "going back" (EU Chamber of Commerce in China, 2016).

However, progress can be detected, e.g. in some services such as retail and wholesale, where liberalisation has enabled European supermarket chains and department stores to establish networks in China. It is also fair to say that China has been making earnest attempts to pursue SOE reforms, especially institutional/structural reforms and greater opening up of some traditionally SOE-dominant sectors to foreign investment. For example, to cut overcapacity, the Baosteel Group Corporation and Wuhan Iron & Steel (Group) Corporation merged to become Baowu Steel Group Corporation on 1 December 2016. Of course, huge social impact was involved in the restructuring, such as mass layoffs. Prior to the merger, it was reported in December 2015 that the Wuhan Iron & Steel Group would lay off 11,000 employees over three months. Some layoffs would be in the form of early retirement and no-pay leave.<sup>16</sup> There must have been layoffs on a similar scale within the Baosteel Group.<sup>17</sup> Given the huge scale of steel overcapacity in China, a range of such drastic measures will be unavoidable. Regarding the long-awaited SOE mixed-ownership reform, which was another decision made at the Third Plenum, it was announced on 27 April that experimental measures for SOEs' mix-ownership would be published soon. However, the announcement continued by saying that "mixed-ownership"

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<sup>15</sup> A word of caution, though. When explaining China's reform plan, which was released by the Xinhua News Agency at the end of the Third Plenum, President Xi did highlight elements such as that the government's role in market reforms would remain, some measures would be studied for suitability, and some for the best approaches for implementation. Moreover, those reform measures at local levels would be implemented more quickly than those at the central government level and a longer period of implementation could be expected. The deadline for implementing the full reform package is 2020. See [http://news.xinhuanet.com/english/china/2013-11/15/c\\_132891949.htm](http://news.xinhuanet.com/english/china/2013-11/15/c_132891949.htm). Having said that, the authors do not suggest that the growing impatience of foreign businesses and the EU is illegitimate. This example of omission, i.e. the government's role and a longer implementing period, indeed raises the question of access to Chinese media (even though the Explanation was released in English by the Xinhua News Agency). Only a fraction of Chinese government policies, announcements, etc., are translated from Chinese to English. Therefore, analyses conducted by foreign academia and media are often based on limited information, resulting sometimes in speculative or out-of-context reporting and conclusions. This could also distort the Chinese government's credibility.

<sup>16</sup> See Xinhua Net (2015), "Wuhan Steel Plant may lay off more than 10,000, officials denied", 15 December. See: [www.gd.xinhuanet.com/newscenter/2015-12/15/c\\_1117461742.htm](http://www.gd.xinhuanet.com/newscenter/2015-12/15/c_1117461742.htm) (Chinese).

<sup>17</sup> It is reported that in 2016 the Baowu Group achieved the best performance in the Chinese steel industry with an operating revenue of RMB 307.2 billion (EUR 40.1 billion) and a profit of RMB 7.02 billion (EUR 0.92 billion). See <http://www.baowugroup.com/en/contents/5273/102759.html>.

reform is not as simple as introducing private ownership to the seven strategic sectors, which include petroleum, natural gas, railways and civil aviation.<sup>18</sup> The notion of reforming SOE ownership dates back to the 1990s. Back then, in order to solve the deficit issue, many SOEs at the central government level began to list a minority of their shares on stock exchanges, e.g. Hong Kong, to attract private capital. The “mixed ownership economy” measures announced by the Third Plenum should change the governance structure of SOEs, encouraging private investors to take a controlling interest and allowing employees to hold shares. Also, at a 31 March press conference Ministry of Commerce Vice-Minister Wang Shouwen provided an update on pilot free trade zones. He announced that so far the management experience obtained in Shanghai has been extended to seven such zones. Note that these pilot free trade zones test new mechanisms such as trade openness, investment liberalisation, administrative and financial institutional reforms, and engaging the negative list approach.<sup>19</sup> The first pilot free trade zone was established in Shanghai in September 2013. By virtue of Art. 12 of Chapter III on Investment Opening of the Regulations of China (Shanghai) Pilot Free Trade Zone (July 2014), the Shanghai Pilot FTA Zone was tasked with experimenting with opening up a number of service sectors such as financial services, shipping services, commercial and trade services, and suspending, cancelling or relaxing investor qualification requirements, restrictions in share ratio of foreign investment and business scope and other special management measures. It is said that the whole package of mechanisms, if successful in the pilot free zones, would eventually be implemented throughout the country. (Of course, in a WTO FTA, the meaning of “free trade zones” is not the same.)

To sum up, the Chinese government announced ambitious reform measures but implementation has been much delayed. It is understood that the government wishes to exercise much caution at this stage of reforms, especially with regard to withdrawing SOEs’ lifeline for operations, i.e. government policy and public finance. Although the deadline set for implementing the full reform package announced at the Third Plenum is 2020, any delayed implementation would cause European businesses, in fact all of China’s trading partners, increased anxiety, casting doubt on China’s credibility. Such a delay also risks impeding China from achieving its economic goals, e.g. transforming to a service-led and higher-value-added economy, fostering closer cooperation with its major trading partners, such as the EU, to unlock greater trade potential, and advancing other trade negotiations.

#### 5.4 China and four WTO plurilaterals

China is facing bottlenecks in its four plurilateral trade negotiations with leading trading partners eager to go beyond regular WTO accomplishments. These plurilaterals are a useful criterion or test of trade leadership. They include Information Technology Agreements nos 1 and 2. For the latter, China in December 2015 agreed to eliminate tariffs on 201 additional IT products, making it a successful member of this revised plurilateral. However, China clearly

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<sup>18</sup> See <http://news.eastday.com/c/20170427/u1a12924962.html> (Chinese).

<sup>19</sup> See <http://interview.mofcom.gov.cn/detail/201704/ff8080815a647627015b273b75f60017.html> (Chinese).

struggles with the negotiations of the Government Procurement Agreement (GPA), the Trade in Services Agreement (TiSA) and the Environmental Goods Agreement (EGA).

China is negotiating for its accession to the GPA after its sixth offer was submitted in December 2014. China has made extensive concessions in its last offer in relation to, *inter alia*, (i) widened coverage of procuring entities and (ii) of the relevant goods, services and works, as well as (iii) lowered thresholds. But China's partners wish to see even more concessions in covered entities, activities and works, with lowered thresholds. The core objection, however, is the status of SOEs: partners want China to offer SOEs and their procuring activities to foreign bidders under the principle of reciprocity, simply because this is what Chinese firms enjoy in the European public procurement market, and largely elsewhere as well. The grievance is growing, as recently expressed by the European Commission, which again raised concerns about the limited access EU companies get to public markets abroad (Michalopoulos, 2017a). In this respect, a good sign for China's possible compromise is that in its sixth offer, activities in the sectors of, for example, energy and postal services are offered for procurement coverage. However, such activities are typically monopolised by SOEs, which are protected from foreign competitors, not least of all investors.

For the TiSA negotiations, China expressed its intention to join but not yet as a negotiating party. It is perhaps not difficult to understand its hesitation given, once again, the SOEs that are so prominent in services markets via regulations and extreme market power. China intends to open up the service sector, as pledged at the Third Plenum, but actual measures are yet to be seen. At the moment, it is far behind in services value added as a share of GDP and some Chinese scholars are calling for transforming the economy so as to become service-led by 2020. One legacy problem is China's industry-led institutional structure. Therefore, becoming a service economy means succeeding at institutional reforms (Fulin, 2015: 144). TiSA negotiations presently take place among 50 WTO members, representing 70% of global GDP. If China joins the negotiations, it would correspond with China's intention to open up its services sectors, per the Third Plenum pronouncement, and facilitate its CAI or FTA negotiations, especially with respect to pre-establishment national treatment.

Finally, the EGA targets reductions in or removal of tariff and non-tariff barriers, such as local content requirements or restrictions on investment, environmental goods and services. The EU also hopes that, once the EGA is finalised, the most favoured nation principle will be applied to all WTO members, so all members could open up their markets. A possible obstacle to China is the opening up of its environment services to fellow EGA parties. Then again, China has become the world's biggest investor in renewables (€58 billion invested in 2012).

## 6. Conclusion

China and the EU have reacted very similarly to recent waves of populism that culminated in a trend of sneaky protectionism and, in particular, Trump's 'America First' initiatives. As shown in Metivier, di Salvo & Pelkmans (2017), the EU has done remarkably well economically in 'its'

globalisation without experiencing great social tensions as adjusting workers in Europe tend to be reasonably well protected in the short term (indeed, more than US adjusting workers). That China has an enormous stake in globalisation is well known, and Xi's elegant speech in Davos confirms this in no uncertain terms. Hence, China and the EU share the same fundamental globalisation interest and can work together, beyond 'policy-making by speech'. The very fact that China and the EU both wish to signal clearly that responsible globalisation is desirable is undoubtedly important for many other trading partners in the WTO.

We have shown that both China and the EU have the manifest ambition to foster (responsible) globalisation in their activist trade and investment strategies. But China is a relative newcomer in building and upholding the world's trade regime; so far, it has managed to implement the principles and rules set down by the WTO. Maintaining if not deepening responsible globalisation requires, in addition to clear ambition as expressed in many interesting bilateral, regional, plurilateral and – if possible – multilateral initiatives, a recognised and credible capacity to exercise leadership by, for example, applying "WTO plus" provisions for greater trade liberalisation. Such a capacity is reflected, on the one hand, in 'leadership by example', by allowing liberal access to its markets and assuming a relaxed position toward global economic intercourse that intrudes on its own economy. 'Leadership by example' matters a lot when it is practised by trade giants such as China and the EU: it is in the direct economic interest of all trading partners, and sends strong signals to other economies.

On the other hand, China and the EU, as leaders in responsible globalisation, should be able to amplify this posture by agreeing to a trendsetting bilateral initiative (that is, a deep and comprehensive FTA and a modern open CAI), whilst taking credible steps to connect and cement other multi-country trade initiatives, whether as plurilaterals, 'open' extensions of TPP-11 and the RCEP, and/or some other means. This – the capacity, not ambition, to exercise trade leadership – is where China has quite a lot of work to do. Our painstaking analysis (Pelkmans et al., 2016) of a possible deep and comprehensive FTA between China and the EU has revealed both significant and myriad barriers to market access on China's part that simply prevent China from leading by example. China is well-advised to narrow the gap between its ambitions and its (thus far) *limited* capacity to deliver on basic elements of such an FTA. With respect to plurilaterals and open extensions of TPP-11 (involving a quest for Chinese membership and even a possible extension to the EU, for those countries not having an FTA with the EU) or of the RCEP, no strategic initiatives seem to be on the horizon at the moment. The EU for its part has now accepted the idea of trying to forge an all-ASEAN FTA, knowing that ASEAN is an important trading partner with China. This will not only be a tall order; it signals that all such possible initiatives are somehow related. The EU and China have every interest in considering these options or variants of them in earnest. Moreover, with China's understandable insistence that the EU be (still) more interested in the Belt and Road Initiative, China has a unique opportunity to demonstrate trade leadership by showing that GPA and other aspects of rules, e.g. on TBTs and customs, respected by 'leading trading partners' should govern contracts and agreements within the Belt and Road Initiative.

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