

# CAN DIALOGUES ADVANCE EU-CHINA TRADE RELATIONS?

## Abstract

The EU pursues its trade agenda with China through a web of economic and sectoral dialogues. We show that these dialogues do matter for wider EU trade policy. After a brief overview of the architecture, we map the trade-related dialogues and identify seven possible functions of them, giving examples of dialogues on public procurement; reforms of state-owned enterprises (SOEs); forced technology transfer; the protection of intellectual property rights; and sustainable forestry and the timber trade. The assessment seeks to answer four specific questions:

- i. Do dialogues improve market access? Dialogues would seem to have facilitated market access in a variety of ways. The EU has also insisted on reforms in China with a view to easing restrictions that hinder effective market access. For some aspects this seems to have worked, but not for the big issues, for example SOE reforms.
- ii. Can the web of dialogues be seen as an ‘unbundled’ free trade agreement (FTA)? The answer is, not really. The trade dialogues do not seem to substitute, even imperfectly, for an FTA.
- iii. Can the dialogues stimulate ‘sustainable development’? A recent convergence of EU and Chinese objectives has been extremely helpful for effective bilateral cooperation, on social matters (labour standards and social protection) and the environment & climate. Cooperation on energy, climate strategies and other environmental concerns, following dreadful neglect and indifference in China, are achieving results, such as better (for instance, risk-based) regulation, higher ambitions and more effective enforcement.
- iv. Can dialogues reconcile or at least mitigate ‘systemic’ differences? Here, dialogues have not proved very useful in terms of results. From the EU end, addressing systemic differences effectively when the partner country takes pride in enjoying a ‘socialist market economy with Chinese characteristics’ is intrinsically impossible. It is an accomplishment when channels of cooperation are kept open.

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## Abbreviations

|         |   |
|---------|---|
| APEC    | Asia-Pacific Economic Cooperation                               |
| ASEAN   | Association of Southeast Asian Nations                          |
| CAI     | Comprehensive Agreement on Investment                           |
| CCP     | Chinese Communist Party   |
| CEN     | European Committee for Standardization                          |
| CENELEC | European Committee for Electrotechnical Standardization         |
| ETSI    | European Telecommunications Standards Institute                 |
| FDI     | Foreign direct investment                                       |
| FLEGT   | Forest law enforcement, governance and trade                    |
| FTA     | Free trade agreement  |
| GI      | Geographical indications  |
| GPA     | Government Procurement Agreement                                |
| IEC     | International Electrotechnical Commission                       |
| ILO     | International Labour Organization                               |
| IPR     | Intellectual property rights                                    |
| ISO     | International Organization for Standardization                  |
| MOFCOM  | Ministry of Commerce  |
| RESPECT | Realising Europe's Soft Power in External Cooperation and Trade |
| SASAC   | State-owned Assets Supervision and Administration Commission    |
| SOE     | State-owned enterprises   |
| SPS     | Sanitary and phytosanitary                                      |
| TBT     | Technical barriers to trade                                     |
| TDI     | Trade defence instrument  |
| VPA     | Voluntary partnership agreement                                 |
| WTO     | World Trade Organization  |

## Executive Summary

The EU pursues its trade agenda with China through an intricate web of economic and sectoral dialogues. Even though the EU conducts dialogues with many trading partners, the sheer total and very wide scope of EU-China dialogues render this approach unique. What is publicly known about these dialogues is incomplete and selective. We show that these dialogues do matter for wider EU trade policy. Moreover, besides traditional technical aspects of trade policy, dialogues have long extended to cover ‘values’ or non-trade policy objectives, including ‘sustainable development’. The EU and China have had dialogues on many aspects of sustainable development, as part of both the ‘social’ and the ‘green’ dialogues, beginning in the late 1990s.

China and the EU have cooperated under a ‘comprehensive and strategic partnership’ since 2003. The partnership is substantiated by an architecture of bilateral dialogues, consisting of three pillars – namely political, economic and sectoral, and people-to-people exchanges. By far the largest pillar is the economic and sectoral one, which is mostly trade related, comprising over 50 dialogues in various forms and intensities.

Today’s architecture for EU-China dialogues can be traced back to a number of original rationales. First were early development needs and requests for policy learning. Second, some initial dialogues were linked to the 1985 EU-China non-preferential trade agreement. Third, was preparation for China’s accession to the World Trade Organization (WTO) – when the EU offered capacity building and support programmes. Finally, there was the persistent urge on both sides for China to reform deeply and structurally as China migrated out of the rigidly planned economy towards a market economy. Currently, the underlying rationale for having so many trade-relevant dialogues is that modern trade and investment policy covers a very broad spectrum of policy areas.

We attempt to assess the roles and influence of these dialogues. This report presents a concise overview of their architecture. It then maps the trade-related dialogues, and identifies seven possible functions of them. In the present (shortened) report, the analysis of these functions is rather compact; therefore, five boxes give specific examples of dialogues to illustrate the varied nature, intensity and results of these arrangements. These boxes discuss public procurement, reforms of state-owned enterprises (SOEs), forced technology transfer, the protection of intellectual property rights (IPRs), and sustainable forestry and timber trade. Most of the report, however, is dedicated to answering four questions on the effects of these trade-related dialogues: i) Do dialogues improve market access? ii) Can the web of dialogues be seen as an ‘unbundled’ free trade agreement (FTA)? iii) Can the dialogues stimulate sustainable development? iv) And can dialogues address ‘systemic’ differences?

### *Do dialogues improve market access?*

Dialogues have facilitated market access in a variety of ways: helping Chinese laws to align with WTO laws; supporting the delivery of specific WTO commitments; strengthening enforcement by China, including technical controls; stimulating an opening-up in specific fields (like air transport and maritime); and assisting China to level the playing field internally, which is also helpful for EU companies in China. On trade defence, there have been two dialogues but the EU has only further increased its restrictions, via its trade defence instrument, vis-à-vis China. The EU has also consistently insisted on reforms in China with a view to easing restrictions that hinder effective market access. In some aspects this seems to have worked, but not in the big issue of SOEs, for example. Notably, China's application of the Anti-Monopoly Law to mergers between large SOEs is plainly anticompetitive. On forced technology transfer, dialogues failed to work and the EU eventually settled for filing a WTO case. On IPRs, however, dialogues and follow-up programmes have been quite successful – the remaining (serious) problem is enforcement. For geographical indications (GIs), a seven-year negotiation resulted in an EU-China agreement in 2019, with the protection of 100 GIs on each side to begin with. On technical standardisation, the partners still have a dialogue on technical barriers to trade, but meanwhile there is also a quasi-permanent, multi-party cooperation initiative, based in Beijing, among CEN (European Committee for Standardisation), CENELEC (European Committee for Electrotechnical Standardisation), ETSI (European Telecommunications Standards Institute), the European Commission and EFTA (European Free Trade Association).

### *Can the web of dialogues be seen as an 'unbundled' FTA?*

The answer is not really. The FTA is no longer a short-run objective for the two partners and the EU's two prerequisites for starting FTA talks have not been fulfilled: concluding the Comprehensive Agreement on Investment and deep reforms in China (bound to include a different approach to SOEs). The trade dialogues do not seem to substitute, even imperfectly, for an FTA, though the dialogue subjects coincide with a number of typical FTA chapters. Indeed, an eventual future FTA may be – in part – conveniently drafted based on some of the dialogues.

### *Can the dialogues stimulate sustainable development?*

In sustainable development, a recent convergence of EU and Chinese objectives has been extremely helpful for effective bilateral cooperation for both the social (labour standards and social protection) and the environmental & climate dialogues. The EU and China have worked together for two or more decades on a myriad of projects, programmes, dialogues, declarations (also through the summits for political impetus) and via special funding. Thus, in recent energy cooperation the bilateral collaboration goes remarkably far; in climate strategies the EU and China have lately come to work closely together, but also did so in the heyday of the Clean

Development Mechanism.<sup>1</sup> On other aspects of the environment dialogue, following dreadful neglect and indifference in China, the cooperation has achieved results, such as better (for instance, risk-based) regulation, higher ambitions and more effective enforcement.

*Can dialogues reconcile or at least mitigate systemic differences?*

For systemic differences, the dialogues have not proved very useful in terms of results, if indeed this can be expected from dialogues. It is already an accomplishment when channels of debate are kept open. From the EU end, dealing with systemic differences effectively when the partner country takes pride in enjoying a ‘socialist market economy with Chinese characteristics’ is intrinsically impossible. This question is so fundamental, if not existential given the overwhelming and highly intrusive role of the Chinese Communist Party, that one can only work pragmatically on the incompatibilities with the WTO and the experienced negative spillovers from the massive interventionism in China. These features are reflected in the EU’s China strategy of March 2019, in which China is regarded as a partner and a competitor as well as a rival.

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<sup>1</sup> More specifically, the Clean Development Mechanism (CDM) of the Kyoto Protocol; the successful and influential cooperation between China and the EU on CDM investment projects is set out in detail in a box in Pelkmans (2020).

## 1. Aim and structure

Even though the EU conducts dialogues with many trading partners, the sheer total and very wide scope of EU-China dialogues render this approach unique. What is publicly known about these dialogues is very incomplete and selective, and there is no intention on either side to change this more than marginally. Nevertheless, there are many signals, apart from occasional hard evidence, that these dialogues do matter for wider EU trade policy. Moreover, besides traditional technical aspects of trade policy, dialogues have long moved further still in order to deal with (what former EU trade commissioner Cecilia Malmstrom calls) ‘values’ or non-trade policy objectives, including ‘sustainable development’. Since the European Commission’s paper on “Trade for all” of 2015,<sup>2</sup> non-trade policy objectives have been recognised as ‘trade relevant’ in the EU. The EU and China have long had dialogues on many aspects of sustainable development, as part of both the ‘social’ and the ‘green’ dialogues, beginning in the late 1990s.

China and the EU have cooperated through a ‘comprehensive and strategic partnership’ since 2003.<sup>3</sup> The partnership is substantiated by an architecture of bilateral dialogues, consisting of three pillars, namely political, economic and sectoral, and people-to-people exchanges. The first and the last pillar together do not even add up to 15 dialogues, whereas the economic and sectoral pillar comprises over 50 dialogues in various forms and intensities.

In the present CEPS report, we attempt to assess the roles and influence of these dialogues. Section 2 provides a brief overview of the architecture. Section 3 maps the trade-related dialogues, and section 4 identifies seven possible functions of them. To keep the report short, the analysis of these functions is rather compact. Therefore, five boxes give specific examples of dialogues to illustrate the varied nature and intensity of these arrangements. Most of the report, however, is dedicated to answering four questions on the effects of these trade-related dialogues, in section 5: i) Do dialogues improve market access? ii) Can the web of dialogues be seen as an ‘unbundled’ free trade agreement (FTA)? iii) Can the dialogues stimulate sustainable development? iv) And can dialogues address systemic differences? Section 6 sums up the conclusions.

## 2. Overview of the EU-China dialogues architecture

Mapping the EU-China dialogues is possibly useful but also complicated due to their proliferation over time and their organic growth without an explicit strategy or (published) guidelines to do so (see Box 1). Moreover, some dialogues operate without any publicity, and other ones with some or regular minutes or press releases.<sup>4</sup> ‘Mapping’ is therefore a

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<sup>2</sup> European Commission (2015), “Trade for all, towards a more responsible trade and investment policy”, Luxembourg: Publications Office of the European Union, October ([www.op.europa.eu/en/publication-detail/-/publication/d90eda7c-7299-11e5-9317-01aa75ed71a1](http://www.op.europa.eu/en/publication-detail/-/publication/d90eda7c-7299-11e5-9317-01aa75ed71a1)).

<sup>3</sup> In fact, under a ‘comprehensive partnership’ since 1998.

<sup>4</sup> Farnell & Crookes (2016) confirm that much of the EU-China dialogues remains unpublished. “Both sides would maintain that confidentiality is a precondition for a frank exchange of views and that greater transparency of these discussions might lead to more defensiveness” (p. 172). John Farnell is a former high official of the European Commission.

cumbersome exercise and certainty about the completeness of a survey remains an illusion.<sup>5</sup> In order to keep the overview manageable for a short report like this, we have chosen to shift the details to a large flowchart in the Annex. The flowchart is an adapted version of one published by the European External Action Service in 2015,<sup>6</sup> which remains broadly valid to date. Almost a dozen new or missing dialogues have been inserted into the original flowchart (all in the second pillar). By slightly compressing the information about the first and third pillars, the focus is put on the second pillar: economic and sectoral dialogues, which suits our purpose.

*Box 1. What is a dialogue in EU-China trade relations?*

There are two ways to understand the nature of a bilateral dialogue. One is to describe what ‘dialogues’ one can observe, the other is to appreciate why and how a dialogue avoids possible alternative ways of conducting diplomacy and yet seeks tangible results. In EU-China trade relations in a wider sense, both ways matter.

First, one can attempt to describe dialogues in their many forms and extent of organisation, levels (in hierarchies), official labels and degrees of permanence. We refer to the Annex and Hu (2020) for more detail. In the case of EU-China, there is no FTA or customs union, so the typical committee structures included in such treaties do not exist. What has essentially happened during the last 25 years of EU-China relations in the wider trade, investment and economic domains is that a dialogue is initiated when the two parties see a need or opportunity. In some specific cases, the dialogues have intensified and eventually transformed into legal negotiations preparing for formal agreements or treaties (e.g. on customs cooperation, geographical indications, maritime and air transport, and the Comprehensive Agreement on Investment (CAI) on which negotiations are still ongoing). Dialogues can be ‘high level’ or not (which does not say much in actual practice), regular (if not annual) or not, linked to technical and practical programmes or projects of all kinds (some of which have been very substantial). Diplomatic wording may matter. For example, by renaming a dialogue and giving the bilateral work a beautiful label (e.g. the Blue Partnership), by delegating sensitive issues to working groups (for instance, on illegal, unreported and unregulated fishing, on World Trade Organization (WTO) reform or on technical rail issues), or by organising the work as a bilateral cooperation mechanism as in the timber trade, the overall dialogue is not damaged too much.

Second, dialogues often begin as typical testing grounds, not legal obligations or rigid frameworks. Indeed, many countries may first seek dialogues and not be interested in ‘hard’ agreements. This is even more true for China, as its long traditions are rooted in relational commitments (often) more than hard legal obligations, which may be perceived as hampering as much as helping, since relationship could be unreliable especially when conflict with national interest arises. Also, trust has to be built up and this is best done in loose frameworks, without too many binding obligations. Moreover, since 2001 China and the EU have both been bound by WTO law and China in addition by its Protocol of Accession to the WTO (with some additional obligations), so the bilateral dialogues need not be burdened by these legal issues. The term ‘dialogues’ and their practice thus far express this more

<sup>5</sup> As is clear from the survey in Hu (2020).

<sup>6</sup> See [https://eeas.europa.eu/sites/eeas/files/2015\\_november\\_eu-china\\_dialogue\\_architecture.jpg](https://eeas.europa.eu/sites/eeas/files/2015_november_eu-china_dialogue_architecture.jpg).

diplomatic and relational approach very well. More importantly, more often than not in EU-China trade and investment relations in a wide sense, it is the combination of confidential discussions and debate without much or any public detail (e.g. a press release or more) that is regarded as helpful or the least-hindering diplomatic relations when seeking pragmatic results. The conviction – strong in the OECD world and some other countries – that dialogues are not so convincing because they lack hard obligations, is not necessarily wrong in some cases. However, the pursuit of hard obligations in trade, investment and, e.g. sustainable development, changes the nature of discussions and might fail or remain very modest for that very reason, whereas EU-China dialogues have accomplished a considerable list of results due to pragmatic cooperation.

The second pillar of the bilateral dialogue architecture is extremely rich and varied. It comprises a wide set of typical trade policy issues, notably:

- consultation on technical barriers to trade (TBT);
- trade defence measures (certainly with China);
- customs issues;
- a range of regulatory trade issues that all have dialogues and/or working groups;
- specialised sectoral dialogues (from competition policy and industrial products to science & technology, sustainable tourism and the dialogue on food safety);
- several dialogues on ocean affairs (later: the Blue Partnership), on fisheries and on the Law of the Sea & Polar affairs,
- a bilateral cooperation mechanism on sustainable forestry & trade (based on the EU FLEGT initiative on forest law enforcement, governance and trade);
- several initiatives and dialogues under the Climate Change Partnership (including the low-carbon economy, smart city and circular economy); and the ambitious Energy Roadmap of 2016, which is full of actions.

In addition are dialogues on state aid control, the Legal Dialogue and the one about, and with, small and medium-sized enterprises. A number of these dialogues have spawned important working groups, like those on the market economy status, on WTO reforms and on illegal, unreported and unregulated fishing, as well as, for example, the specialised Railway Working Group.

Deliverables from dialogues are summarised in the annual China-EU summit, which also announces the respective work programmes for the next steps. The many implementing projects pursuing the different objectives of dialogues render the bilateral, comprehensive strategic partnership concrete and substantive. The summit, in turn, supports the dialogues with political blessing, and resumes personal contacts among the leaders and their cabinet members, which is important for building trust.

‘Below’ the summit, there are several very broad high-level dialogues involving the Commission vice president and China’s vice premier, supported in turn by meetings of top officials. A special case is the bilateral Connectivity Platform prompted by the Belt and Road Initiative, only launched in 2015, which is conducted at the political level and with working group meetings

among experts.<sup>7</sup> The same format is applied by many economic and sectoral dialogues, from the High-Level Economic and Trade Dialogue to the Dialogue on Food Safety, which is conducted between specialised departments as well as working parties and committees. Some dialogues are conducted at both political and working party levels simultaneously.

Overall, it would seem that the entire ‘conglomerate’ of dialogues is highly decentralised, where form is a function of substance and the variable demand for detail. Still, it must be borne in mind that, especially on trade relations, the overall cooperation between the EU and China was designed to be open and broad, ever since the 1985 Trade and Economic Cooperation Agreement. Such a relationship was intended to not exclude any subjects of economic cooperation as long as they fell within the (then) competence of the European Economic Community (Article 10).

### 3. Trade-related EU-China dialogues

Given the large number of economic and sectoral dialogues, it is necessary to first identify which dialogues are ‘trade related’ or indeed ‘trade-policy related’.

Figure 1. Trade relevance of EU-China dialogues

#### Strategic

- High Level Econ & Trade Dialogues

#### Direct trade-relevant dialogues

- Joint customs cooperation (agreement)
- Industrial products & WTO /TBT
- Pharma & medical devices
- IPRs, incl. GI, & enforcement
- TDI best practices WG
- ICT/ Telecoms Dialogues
- Agricultural Dialogues
- Fisheries Dialogues
- Dialogue on consumer products (safety)
- Animal health dialogue (MOU)
- Trade & Investment Dialogue
- Economic / Trade WG
- Market-economy status WG
- High-level Transport Dialogue
- Dialogue on Food Safety / SPS
- Maritime Transport (Agreement)
- Reg. dialogue on Public Procurement
- Ocean Affairs (Blue Partnership)
- Law of the Sea & Polar affairs
- BCM on sustainable forestry & trade
- EU/China WG on IUU
- EU/China WG on WTO Reform

#### Other trade-relevant dialogues

- Competition policy dialogue
- Railway WG
- Labour, employment, social affairs dialogue
- Industrial sectors dialogue / consultation
- Drug precursors Joint follow-up WG
- Energy Security (Declaration) & Energy Roadmap
- Climate Change Partnership
- Environmental Policy Dialogues
- Electricity market Dialogue
- H & S (occ. HS) Dialogue
- Sustainable Tourism [Mode 2, GATS]
- State-aids control

#### Other economic dialogues

- 12 X might be trade-relevant (e.g. macro-economic; High-level dial. on Innovation Cooperation; High-tech sectors; Science & Technology; Legal/rule-of-law; Low Carbon economy; SME policy; Health)
- 8X non-trade (e.g. urbanization; High-level Dial. on Circular Economy; smart city)

#### Connectivity Platform

Source: “EU-China Dialogue Architecture”, European External Action Service, November (2015) and authors’ compilation.

<sup>7</sup> See the projects presented under the EU-China Connectivity Platform ([https://ec.europa.eu/transport/themes/international/eu-china-connectivity-platform\\_en](https://ec.europa.eu/transport/themes/international/eu-china-connectivity-platform_en)).

In Figure 1 we distinguish between directly trade-relevant and indirectly trade-relevant dialogues, allowing yet another category comprising 12 dialogues that *might* at times be trade relevant, besides the special Connectivity Platform which surely is trade relevant (but heavily oriented towards infrastructure).

No fewer than 22 dialogues are directly trade relevant and another 12 have indirect trade relevance.<sup>8</sup> In addition, another 12 of the 20 remaining economic dialogues *might* have trade relevance on occasion, such as the macroeconomic dialogue, the one on high-tech sectors, the legal one (e.g. on the rule of law) and the low-carbon economy. Altogether, this adds up to 46. And there is the increasingly important Connectivity Platform with its emphasis on infrastructure (rail, air, road and digital connectivity), technical standards, customs facilitation and regulatory issues which dictate that the operation of the Belt and Road Initiative in the EU must respect the single market rules.<sup>9</sup> In short, there is a widespread bilateral ‘web’ of EU-China dialogues, including some that would not always be considered part of trade policy but which matter for bilateral and multilateral trade and investment.

#### 4. Functions of EU-China trade dialogues

The difficulty in mapping the EU-China dialogues is that, through organic growth, dialogues may generate new dialogues when, for example, the importance or coverage of a single issue increases so much that it might engender other new dialogues in their own right. Such organic development can take place across the various competences of the directorate-generals at the Commission, and the whole structure appears complicated. Nevertheless, it seems possible to identify no fewer than seven functions of the dialogues, as summarised in Table 1.

*Table 1. Seven functions of EU-China trade dialogues*

|    |     |   |
|----|-----|---|
| 1. |     | Exchange of information, better understanding and mutual (policy) learning  |
| 2. |     | Capacity building   |
|    | 2.1 | Project-based activities to tackle challenges and for mutual learning   |
|    | 2.2 | Exchange of staff & close cooperation between agencies/services   |
|    | 2.3 | Capacity building & implementation support  |
| 3. |     | Trade policy-related consultations, pre-negotiations and coordination for international fora  |
|    | 3.1 | Joint efforts/‘undertakings’ in multilateral/international cooperation  |
|    | 3.2 | Technical consultation on (many) bilateral trade & investment aspects   |
|    | 3.3 | Identifying solutions to issues of mutual interest, e.g. preparing technical negotiations or agreeing on memoranda of understanding |

*Source:* authors’ compilation.

<sup>8</sup> We recognise that this distinction is not always sharp to draw.

<sup>9</sup> See Blockmans & Hu (2019).

Table 1 is to be read keeping in mind the enormous changes in the economic, social, legal, institutional and technical capabilities of China over the (say) 25 years of the dialogue process. One prominent difference between the 1990s and today is that the EU and China have neither a donor-recipient nor a mentor-disciple relationship, but a multifaceted partnership<sup>10</sup> between two mature economies as equal partners. Moreover, China's capacity in legislation and technicality of requirements has made tremendous progress over the past decades, indeed so much so that the country has much to offer for the EU to learn. The contrast over time matters when inspecting the three main functions under item 2. However, this does not mean that functions under item 2 are no longer exercised. Under item 2.1, for example, funding is nowadays often provided by both the EU and China. Joint agenda-setting has also become more of a common practice, though China would prefer to be able to exert more influence on this. Not only has China changed over time, but also the EU has – though less spectacularly – whether in policy priorities or in deepening or improving a range of policies relevant to trade and investment.

Based on Hu (2020), it is instructive to look at some examples under the various items in Table 1. Under item 1 (exchange of information), a permanent feature is domestic reforms in China. China and the EU have cooperated on many different domestic reforms for over two decades.

*Box 2. Regulatory Dialogue on Public Procurement*

It was only in 2000 that China enacted its public procurement laws, in order to qualify for WTO membership. Prior to that, public procurement activities were 'centrally planned' and had little relevance to trade. They were also closely linked to state-owned enterprises. Given the nature of China's interventionist traditions even after central planning was given up, open and transparent public procurement has proven to be a difficult issue to tackle. Traditionally, public procurement has not been a trade issue for China, perhaps not even a 'market' issue, but a problem of public finance whereby the use of public funds would trigger the application of the public procurement rules. Such rules and their supervision would minimise corruption and adverse choices as well as reduce the waste of public money.

In any case, in 2006, a year before China submitted its initial GPA<sup>11</sup> accession offer to the WTO, the Regulatory Dialogue on Public Procurement was set up between China's Ministry of Finance and the DG Markt of the European Commission. The dialogue has the mandate to serve as a forum for policy consultation and discussion, in order to enhance technical expertise and capability in the area of government procurement policy at China's Ministry of Finance. The dialogue was expected to increase mutual understanding and awareness of current and forthcoming policy approaches, legislation and related issues, both in China and in the EU. According to the mandate in details, the dialogue identifies mutual interest, which

<sup>10</sup> In "EU-China – A strategic outlook", the EU describes China as "a cooperation partner with whom the EU has closely aligned objectives, a negotiation partner with whom the EU needs to find a balance of interests, an economic competitor in the pursuit of technological leadership, and a systemic rival promoting alternative models of governance." See EU-China – A strategic outlook, JOIN(2019) 5 final, Strasbourg, 12 March.

<sup>11</sup> The WTO Government Procurement Agreement, which China has committed to join.

enables China and the EU to share their experiences and follow new developments in legislation and enforcement of domestic government procurement rules (including the use of electronic procurement) and in international fora such as the WTO GPA. To achieve these objectives, the overall dialogue format consists of regulatory dialogue, seminars and joint studies to explore solutions in order for China to accede to the GPA in an expeditious manner.

Though China's seventh offer submitted in October 2019 was still considered inadequate because in a number of critical areas (including thresholds, entity coverage and exclusions), the professed openness was still not commensurate with what GPA parties offered,<sup>12</sup> in recent years a number of procurement methods have been adopted by China. One such is e-procurement, probably inspired by the EU's e-procurement strategy, which has been emerging since 2012. This progress is a great leap forward given the historical background of China's public procurement regime, which was a confidential subject accessible only within the governmental establishments, also in relation to the enhanced accountability of the government to its people.

Essentially, a spirit of transparency is being introduced in government expenditures while in the past it was strictly kept within government, a legacy of a centrally planned economy. Along with the introduction of e-procurement methods, government procurement opportunities at different administrative levels are now streamlined and listed on a website. E-procurement has also brought public scrutiny to public procurement, breaking down the secrecy around it and thereby helping to eliminate possible nepotism and corruption. China has also implemented the public-private partnership model for better efficiency when using public funds and when executing larger, complex procurement contracts of longer duration (e.g. maintaining a toll road for two decades or running a metro system, as a Hong Kong company does in Beijing). This is a remarkable development: public procurement is now open for public scrutiny, including judicial review, and the private sector is eligible to participate. As a result, the government has relinquished some of its administrative power, including that of monopoly. The EU has contributed much expertise and influence to this revolutionary process of modernisation of China's public procurement regime through the dialogue platform.<sup>13</sup>

Under item 2, intense and sustained activity in many areas has been reported. Examples under 2.1 include mutual access to funding, publications and research under the High-level Dialogue on Innovation Cooperation; a big and diversified programme of capacity building called the China-EU Trade Project; the opening of the China Window in the Erasmus Mundus programme; and early common initiatives in higher education leading to the establishment of the China-Europe International Business School and the Europe-China Law School. Item 2.2 (personnel exchanges) was an exercise more often used in the early days of bilateral cooperation. For

<sup>12</sup> See the United States Trade Representative (2020), "2019 Report to Congress on China's WTO Compliance", United States Trade Representative, Washington, D.C., p. 38.

<sup>13</sup> See Pelkmans & Hu, et al. (2018), *Tomorrow's Silk Road, Assessing an EU-China Free Trade Agreement*, Rowman & Littlefield (2<sup>nd</sup> ed.), pp. 157; 293-9.

example, secondment took place between China's national intellectual property office and the European Patent Office. Between the Commission's DG Trade and its Chinese counterpart MOFCOM, one famous intern was Wang Shouwen, presently vice trade minister and China's deputy international trade representative. With respect to item 2.3 (capacity building and so on), one can mention a successful chain of programmes on intellectual property rights (IPRs) (since 2004, including working group meetings with stakeholders), detailed technical support and training for verification and control of animal diseases in many Chinese harbours, direct collaboration between EU and Chinese consumer protection authorities on the safety of consumer goods imported from China,<sup>14</sup> and highly specific implementation support for customs followed by more intensified cooperation (and a customs agreement). Such intensified cooperation involved, for example, the improvement of supply chain security and facilitation for reliable traders. The mechanism of smart and secure trade lanes was launched in 2006 in order to test the security measures applied to shipments and containers throughout the journey. Customs cooperation also covered the facilitation of better data exchange as well as mutual recognition on key customs issues.

Under item 3 of Table 1 (which includes identifying solutions to challenges), activity has increased significantly over time, ever since China's membership of the WTO and even more so since China's economic strength has grown and the country has become a leading world trader. As far as the common efforts on international cooperation are concerned (3.1), examples are the joint long-run support of ITER (the nuclear fusion project) now established in France, the bilateral Working Group on WTO reform initiated in 2018, the sensitive collaboration with China in the Global Forum on Steel (though China quit the Forum in autumn 2019)<sup>15</sup> and close cooperation in the run-up to the 2015 Paris Agreement on Climate Change and in the Climate Change Partnership. As far as item 3.2 (technical consultations on specifics of trade policy in the wider sense) is concerned, many of the often highly technical subjects in Figure 1 marked as having "direct trade relevance" can be mentioned. Of course, it is known that the preparations for negotiations do not always work out, as for instance is the case with the 'market economy' status under EU trade defence.<sup>16</sup>

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<sup>14</sup> This is linked to the RAPEX alert system, fed by the EU and its member states. Risky products are traced back to Chinese producers with the help of the authorities and remedies are proposed.

<sup>15</sup> It should be noted that, according to the OECD *Economic Survey of China* (2019, p. 15), China's steel production capacity decreased by just a modest 9.8% over 2014-17.

<sup>16</sup> And since, by virtue of Section 15(d) of its WTO Accession Protocol, China was not confirmed as a market economy by the EU. Because the old methodology for dumping margin calculations expired 15 years after China's WTO accession, in December 2017, the EU updated its methodology by using undistorted benchmarks to determine the 'normal value' of the product. This applies to all WTO members where "significant market distortions" are found. In other words, the notions of a market or non-market economy are no longer employed. What is relevant is evidence on 'significant distortions'. The new regulation has not been recognised by China as WTO-consistent and a formal complaint was lodged to the WTO Dispute Settlement Body. China's complaints focused on the new methodology that the EU has introduced pertaining to the determination of normal value for "non-market economy" countries in anti-dumping proceedings involving products from China. A panel was

## 5. Queries about the effects of trade-related dialogues

An assessment of the usefulness of EU-China dialogues remains difficult because there is insufficient (hard and verifiable) information and officials on both sides are not forthcoming – retreating into diplomatic parlance that remains vague – or are outright silent. The following discussion is based on painstaking research but we are conscious of what we do not know at this stage and are painfully aware of subjects for which there seems to be no way of knowing. Given the great importance of EU-China trade and investment relations, also in the wider sense (i.e. including sustainable development), we have nonetheless pursued this work in earnest. We pose four questions about the actual or possible effects of these dialogues and answer them to the best of our ability and information.

### 5.1 Do dialogues improve market access?

#### 5.1.1 *The general picture*

Here the picture would seem to be mixed and requires careful discussion. Given the many functions of dialogues, some have (over time) been helpful in at least five ways. First, dialogues have contributed to aligning domestic laws in China with WTO rules, and, more importantly, helped to enable the delivery of China's WTO commitments on trade and investment. Examples include IPRs, competition law and the law on technical standardisation. Second, they have helped to strengthen enforcement, sometimes in a very concrete and 'hands-on' fashion (e.g. the close cooperation by EU and Chinese consumer protection authorities to trace producers of overly risky goods and to approach them). Third, the EU has helped to bolster various types of technical controls or supported their convergence with international practices and/or make them identical within the large Chinese market (e.g. in harbours) so as to level the playing field. This has been particularly the case with sanitary and phytosanitary (SPS) types of controls, which is surely one driver of the rapid increase in EU food exports to China over the years. Fourth, dialogues have helped or stimulated an opening-up in specific fields, notably in air transport and to a lesser extent in maritime transport. Fifth, in some cases, the EU has used dialogues to stimulate Chinese authorities to reduce intra-Chinese market fragmentation and uncertainty. This exercise is especially useful to help China level domestic markets after certain monopolies of state-owned enterprises (SOEs) were abolished, and the commercial roles of multi-layered administration in the markets were (supposed to be) relinquished. The establishment of a new market system was imperative, but not necessarily equal or equivalent in the various provinces.

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subsequently established. Nonetheless, on 7 May 2019, the panel received a request from China to suspend the panel's work in the proceedings on European Union – Measures related to Price Comparison Methodologies (WT/DS516), until further notice. More recently, the EU has intensified pressure, holding essentially that China causes 'systemic trade issues' that have to be addressed urgently. See also Pelkmans (2018) for an analysis of the systemic trade issues with China.

### 5.1.2 Tariffs and tariff-rate quotas are dealt with in Geneva

Classical market access with the help of duties<sup>17</sup> levied at the border is of course *not* the subject of EU-China dialogues. A number of dialogues had as their initial purpose to assist China in delivering its WTO commitments, and to support a smooth transit from a centrally planned to a market economy.<sup>18</sup> Tariffs and tariff-rate quotas are left to the WTO agreements or to eventual FTA negotiations, not to dialogues. Also, given China's active unilateral (applied) tariff policy, as set out in some detail in Pelkmans & Hu, et al. (2018), any attempt to improve market access via EU-China dialogues in other ways is bound to remain at best very partial and its effectiveness for EU exporters a priori unclear. Since market access to China is, on the whole, far more restricted than Chinese access to the EU,<sup>19</sup> the dialogues cannot but be a weak and questionable instrument for this purpose. Moreover, despite China's efforts in eliminating market access barriers as seen from its Foreign Investment Law (which came into force in January 2020), there are still numerous Chinese restrictions on incoming foreign direct investment (FDI) and the post-establishment business options, again something that Chinese FDI in the EU hardly encounters as the EU regime is among the most liberal in the world according to the OECD FDI restrictiveness index.

Market access is also influenced by trade defence measures. It should be noted (see Figure 1) that two closely related topics used to have their own EU-China dialogues: trade defence such as anti-dumping and countervailing duties,<sup>20</sup> and the 'market economy status'. For China, there can be no doubt that EU trade defence has been a serious problem for at least a decade or more, even when the total trade value affected is barely more than 1% of bilateral goods trade. In the period 1995-2014, China was targeted by the EU for anti-dumping case initiations for on average some 28% – the highest share among trading partners – but (when taking anti-dumping measures *in force*) the Chinese share of all anti-dumping measures of the EU quickly rose after 2001 to reach 47% in 2014.<sup>21</sup> In 2018, however, the share of anti-dumping measures in force hitting Chinese exporters to the EU (as a percentage of all measures for all trading partners) reached an extremely high 71% (85 of 120),<sup>22</sup> in part due to the steel crisis in China. At the plurilateral level, this was also addressed in the Global Forum on Steel. Additional sensitivity

<sup>17</sup> Or tariff rate quotas in agriculture.

<sup>18</sup> Although it might be discussed at the highest level dialogues, but this is not reported.

<sup>19</sup> See for detail in many aspects of tariffs and regulation, Pelkmans et al. (2018), op. cit.

<sup>20</sup> Safeguard measures also fall under trade defence but these are very rare in the EU (in contrast to the US).

<sup>21</sup> See Pelkmans et al. (2018), op. cit., p. 80. See also Yalcin et al. (2016). In numbers, the US and India had even more anti-dumping cases against China in force at the time.

<sup>22</sup> See European Commission (2019), Annex O, 37<sup>th</sup> Annual Report from the Commission to the Council and the European Parliament on the EU's anti-dumping, anti-subsidy and safeguard activities and the use of trade defence instruments by third countries targeting the EU in 2018, SWD(2019) 141, 29 March ([www.trade.ec.europa.eu/doclib/docs/march/tradoc\\_157811.pdf](http://www.trade.ec.europa.eu/doclib/docs/march/tradoc_157811.pdf)). The 38<sup>th</sup> EU anti-dumping report (of April 2020) shows that this extreme focus on China has stayed the same: 86 measures of a total of 121. See European Commission (2020), Annex O, 38<sup>th</sup> Annual Report from the Commission to the Council and the European Parliament on the EU's anti-dumping, anti-subsidy and safeguard activities and the use of trade defence instruments by third countries targeting the EU in 2019, SWD(2020) 71, 30 April ([www.trade.ec.europa.eu/doclib/docs/2020/may/tradoc\\_158734.PDF](http://www.trade.ec.europa.eu/doclib/docs/2020/may/tradoc_158734.PDF)).

emerged because China had firmly counted on the ‘market economy status’ clause in EU anti-dumping being removed, as legally required by the WTO Accession Protocol, by December 2016. This cannot be discussed in the present context but the practical effect of this clause (more precisely, when market economy status would not be granted in an anti-dumping case) was that the anti-dumping duties imposed by the EU would tend to be some 15-20% higher. The EU replaced this clause with a reform in which market-based comparison of relevant prices would not be accepted for purposes of anti-dumping cases if export companies operate from an economy with ‘significant distortions’. A special EU-China dialogue was established to enable extensive bilateral discussions but as far as we know, to little avail.<sup>23</sup>

### 5.1.3 Market access as a result of reforms

‘Effective market access’ was attempted in other dialogues with, so it seems, modest success. The Chinese reforms that the EU has typically been interested in tend to have the effect of facilitating effective market access in various ways. Many of these issues are complex and cannot possibly be dealt with here in an analytically satisfactory fashion. The crux has often been to render sectors or interventions more ‘market oriented’ (e.g. with fewer restrictions on services), thereby facilitating ‘ordinary’ competition within China between foreign companies and local ones, whether SOEs or private firms. Although the fewer-restrictions approach has worked to some degree, be it at a slow pace, it cannot easily be attributed to EU-China dialogues as such. Rather, the dialogues may have stimulated debates within the Chinese government and helped the government overcome resistance from protected companies, not seldomly SOEs. The EU has also tried to suggest alternative solutions that would be less or not restrictive. Another permanent reform issue in dialogues has been the EU’s insistence on removing the privileges for certain Chinese SOEs. In doing so, effective market access in a range of sectors would surely improve (e.g. banking and insurance). But there is little doubt that one of the major systemic differences between China and market economies is precisely found here. As a consequence, China has been anything but forthcoming on this ‘reform issue’ even in informal dialogues.

#### *Box 3. SOE reforms*

Since 2013, with President Xi Jinping in charge, SOEs have become *more* important and have received increasing support. Two major examples demonstrate this. One is that SASAC (for central-level non-financial SOEs) and Central Huijin (for financial institutions) act as regulators, investors and operators. As Lardy (2019) has shown, the increased support to SOEs clearly is at the cost of loans extended to private firms. Whereas the share of loans (for non-financial enterprises) provided to private firms in China fell from an average of some 52% over the years 2010-13 to a mere 11% in 2016, that to SOEs shot up from 35% in 2013 to no less than 83% in 2016. No wonder the rate of investment of SOEs reacted with a rise (after a delay of two years) from 32% in 2015 to 37% in 2017. Also, the growth of Chinese industrial

<sup>23</sup> As noted, China filed a WTO case against the EU in the light of some clauses in the new EU regulation. See footnote 17.

output attributable to SOEs (which had fallen to a very low rate of 2% by 2015!) showed a hike to 7% by mid-2018.<sup>24</sup>

The other example is found in Chinese competition policy. China's Anti-Monopoly Law of 2007 takes EU competition law as its main reference point, as the Anti-Monopoly Law regulates against anti-competitive agreements, abuse of dominant position and concentration, which are echoes of Articles 101 and 102 of the Treaty on the Functioning of the European Union and the EU's Merger Regulation. This is a result of intense collaboration under joint projects and an active dialogue of the kinds specified in Table 1 as 2.1 and 2.3. But these rules are not applied to SOEs, especially not when mergers are at stake. It is well known that SOEs are far less profitable than private Chinese companies. Some SOEs are 'zombies', which could not persist in a competitive market economy. Such SOEs typically never die but are kept afloat with 'actionable subsidies' possibly (according to the WTO Agreement on Subsidies and Countervailing Measures) and other special arrangements. Eventually, these SOEs are forced to merge with other SOEs. The notion that either they die (possibly with a good social plan) or are bought up by private enterprises (whether Chinese or foreign) and restructured, is so far alien to the Chinese regime. In a period of barely two years, SASAC listed no fewer than 12 bilateral mergers, all of large to very large SOEs.<sup>25</sup> Not only does this practice violate core principles of a market economy, it also ignores the very essence of the Anti-Monopoly Law and may well create or strengthen dominance, a leading reason to forbid or condition the merger. There is a considerable risk that formal entry, when liberalised, cannot be exploited by EU enterprises in the Chinese market in the presence of so much market power.

These features show in no uncertain terms that, despite the significant influence the EU has had on Chinese competition law and its officials, the dialogue has proved futile in the face of a determined regime eager to bolster the role of SOEs in China.

Yet another reform strongly and repeatedly advocated by the EU is about various aspects of investment access and, more generally, about extending 'national treatment' to EU (or foreign) investors. Here the EU business community in China – usually prudent – began to complain aloud about what was called the Chinese fairytale of 'unfulfilled promises'. In the Boao Forum for Asia of 2018, President Xi promised once again that national treatment would be extended to all foreign investors. Only in the April 2019 EU-China summit, however, was this promise becoming more concrete in the framework of the CAI negotiations. If the CAI were to be concluded and ratified, it would surely be a monumental achievement. No other country (e.g. the US began such negotiations five years earlier, but were then suspended) has so far accomplished this. Since the EU is a major player, one may regard this possible success as a firmer change towards greater market orientation, but at present this is still speculative.

<sup>24</sup> Growth of industrial output attributable to private firms fell almost linearly from 25% in 2005 to 7% in 2018.

<sup>25</sup> See [www.sasac.gov.cn](http://www.sasac.gov.cn) and Lardy (2019) for details; the period referred to is June 2015 to August 2017.

*Box 4. Forced technology transfer*

There is much talk and indeed considerable policy friction about China's tactics of forced technology transfer for (e.g. EU) companies interested in investing in China. But we view this as more of an investment issue, and with regard also to IPR protection and parties' freedom of contract. Ever since the early days of China's opening-up, the mentality of Chinese officials has been to seek 'deals' in the 'market for technology'. Examples include foreign companies' parting with technology in exchange for market access in China and using technology transfer in exchange for favourable treatment like reduced fees for land leasing or a waiver of utility charges (this does not mean that Chinese companies do not pay for new technologies, China is in fact one of the world's biggest payers for technologies. China paid €30.80 billion for licensing fees and royalties for the use of IP in 2019).<sup>26</sup>

These tactics were detected long ago and according to China's WTO Accession Protocol, China pledged to eliminate or bring into conformity with the WTO agreement all special trade arrangements, including barter trade arrangements as specified in the protocol.<sup>27</sup> In Annex 1 of the Protocol, China pledged to abolish technology transfer requirements in order to comply with the WTO Agreement on Trade-related Investment Measures (TRIMs), but that is only with regard to trade in goods. At the same time, for example, the subsidies provided for preferential income tax treatment to enterprises transferring technologies must be notified in accordance with Article 25 of the Agreement on Subsidies and Countervailing Duties.<sup>28</sup> The EU (with Japan) at long last joined the US in its complaint, China — Certain Measures Concerning the Protection of Intellectual Property Rights (DS542), which was eventually submitted to the WTO in March 2018.<sup>29</sup> The EU also lodged its own complaint against China on forced technology transfer.<sup>30</sup> Since the Sino-America trade war started, China has made attempts to rectify the bad practice, as seen in its new Foreign Investment Law (Article 24). It is also addressed in the US-China Economic and Trade Agreement of January 2020.

A range of other reforms possibly stimulated and helped by EU-China dialogues consists of more technical reforms that nonetheless are critical for 'effective market access'. Two important examples include technical standardisation and IPRs. As described in some detail in Pelkmans & Hu, et al. (2018, ch. 9), the Chinese technical standardisation system initially suffered from path dependency going back to the days of mandatory planning in a closed economy. This was increasingly at odds with the requirements of a modern and far more open market economy, for both imports and exports of goods (and, at first, especially for

<sup>26</sup> State Administration of Foreign Exchange (SAFE), [International trade in goods and services of China \(02.2020\)](http://www.safe.gov.cn/en/2019/0926/1568.html) (<http://www.safe.gov.cn/en/2019/0926/1568.html>).

<sup>27</sup> See Accession of the People's Republic of China, WTO, WT/L/432, 23 November 2001, at p. 4.

<sup>28</sup> See Annex 5, Accession of the People's Republic of China, WTO, WT/L/432, 23 November 2001.

<sup>29</sup> Though based on the two communications from the chairperson of the panel dated 3 March and 8 June 2020, due to consecutive requests by the US to suspend the proceeding of the panel in light of its ongoing consultations with China, the proceeding has been suspended.

<sup>30</sup> China — Certain Measures on the Transfer of Technology, DS 549.

intermediates). Also, the swiftly rising level of technology in China and the exports of medium- and high-tech goods created a strong demand for conformity assessment based on world standards, or at least on technical standards from the US bodies and from the EU system based on the new approach and on harmonisation. One form of path dependency entailed a myriad of ministries and agencies having a partial say on some forms of standardisation, while at the same time companies formally having no right to standardise. Indeed, conventional market-driven (private) standardisation bodies as referred to in the annex of the WTO TBT Agreement do not exist in China.

In 2015, China finally embarked on a thorough reform of the standardisation system, overhauling the incredible complexity and cutting overlaps, while allowing some freedom for enterprises. In 2017, a new standardisation law was adopted. The EU has worked with China through a dialogue and with a local representation of CEN/CENELEC/ETSI (also funded by the Commission) in Beijing since 2014. China has gradually become more open to consultation with foreign business in the case of numerous standardisation plans; it has also announced its intention to become more active in ISO/IEC, helping to write world standards, again strongly advocated by the EU. Still, it has not stimulated the establishment of ‘private standard-setting bodies’ as defined in the TBT Annex. In other words, standards are still very much state affairs, be it in a more open and rational framework.

One of the most successful dialogues with China for decades is the one on IPRs (Pelkmans et al., 2018, ch. 13; Hu, 2018) as explained in Box 5.

#### *Box 5. IPR protection*

After an initial focus on IPR laws and implementation, including geographical indications (GIs), the emphasis has recently shifted to enforcement via special IPR courts (now functioning in several important cities in China) and technical support in the fight against counterfeiting. That fight is a huge problem still today, with the EU (and its business) suffering major damage every year simply because Europe is the commercial leader in most of the (luxury) product sectors typically suffering from counterfeiting. Less known is that counterfeiting is a huge issue also within China and a lot of litigation takes place. For the EU, of all the counterfeiting discovered at EU borders no less than 56% originates directly from China and several indirect routes probably add another 10% or more. It is estimated that 12.5% of all goods trade from China consists of counterfeited goods!<sup>31</sup> Therefore, despite the active and systematic approach and support through the IPR dialogue, successful in helping China’s law-making and enforcement strategies, one can nevertheless argue that the results of the IPR dialogue are mixed. This is because of the continued failure to come to grips with the massive violation of IPRs in goods trade and within China (also a major problem for EU companies selling there).

But on the other hand, for instance, China has adopted the EU’s *sui generis* GI protection scheme. The conclusion of the bilateral GI protection and cooperation agreement at the end

<sup>31</sup> See European Commission (2018), Report on the EU customs enforcement of intellectual property rights: Results at the EU border, DG Taxation and Customs Union 2018, Luxembourg: Publications Office of the European Union.

of 2019 will further boost the EU's agri-food exports to China, now the EU's second largest agriculture export market after the US, and the export volume is continuously growing. And China is the EU's 5<sup>th</sup> source of imports of agriculture and fisheries (Hu, 2018). Indeed, one hardly hears European farmers complain about China.

Altogether, there is no doubt that reforms in China have, in and by themselves, helped to improve effective market access for EU exporters and investors, but the overall picture is mixed with good and bad experiences. Dialogues clearly play a role in this.

#### 5.1.4 *Dialogues for increasing effective market access*

In a fragmented way, there are documented indications of the role of trade-related EU-China dialogues in the improvement of market access. We use quotations from two EU trade barrier reports to substantiate the point. In the 2013 report,<sup>32</sup> on p. 6 the Commission writes that these “market access issues have been elevated to key priorities in the EU’s bilateral trade relations” and it “has systematically raised them in all bilateral meetings, often up to the highest bilateral political level (e.g. summits)”. In the same report, there is a revealing section (pp. 16-17) on the value of diplomatic (e.g. non-legalistic) trade discussions, not unlike the typical Chinese appreciation of ‘relational’ approaches, in order to solve frictions or overcome market access barriers.

Trade diplomacy is part of the EU’s coherent approach on external action. Trade diplomacy is usually the fastest way to tackle trade barriers as it does not require a specific context, as in the case of FTA negotiations or a long and complex litigation strategy as in the case of trade disputes. ... [S]uch a way to address trade barriers is indeed a diplomatic tool as its objective is precisely to solve issues, suggesting that no party has to lose while the other wins. This avoids the risk of escalation in the disputes and retaliatory measures, legal or not. ... [T]he EU’s capacity to provide convincing alternative solutions, concrete proposals, ideally based on its own experience and the wealth of experience in its Member States and lessons-learned. Regulatory cooperation or dialogues are a very useful tool to do so.

In the 2018 barriers report<sup>33</sup> (p. 15), there is a specific list of dialogues that have been instrumental in addressing market access questions with China:

While the EU has used all avenues to address the challenges it faces with China, including bilateral dialogues (Economic and Trade Working Group, ICT Dialogue, Cyber Task Force, Trade and Investment Dialogue, High Level Economic Dialogue, summit) and multilateral fora (various WTO committees), the recent developments require additional, well-coordinated efforts to better address market access issues vis-a-vis China.

<sup>32</sup> European Commission (2013), Trade and Investment Barriers report 2013, COM(2013) 103, 28 February ([http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc\\_150742.pdf](http://trade.ec.europa.eu/doclib/docs/2013/march/tradoc_150742.pdf)).

<sup>33</sup> European Commission (2019), Report on Trade and Investment Barriers 2018, June ([www.trade.ec.europa.eu/doclib/docs/2019/june/tradoc\\_157929.pdf](http://www.trade.ec.europa.eu/doclib/docs/2019/june/tradoc_157929.pdf)).

It is also interesting to observe (on p. 29) that bilateral dialogues<sup>34</sup> sometimes do lead to issues being resolved, as for instance with SPS standards for cheese in China.

## 5.2 Can the web of dialogues be seen as an ‘unbundled’ FTA’?

Given the Annex and Figure 1 and the many examples mentioned, and given the many trade disciplines covered by the dialogues, one may ask the question of whether the web of (trade-related) dialogues serves as an ‘unbundled’ FTA, without a formal treaty. Of course, the history of a number of trade-related dialogues goes back to the run-up of China’s WTO accession and thus the areas covered coincide with the WTO trade disciplines. There is also a legacy of the 2007-11 negotiations on a Partnership and Cooperation Agreement<sup>35</sup> between the EU and China, which failed but amounted to an exercise almost similar to FTA talks. The notion of an unbundled FTA is not as strange as it might sound.<sup>36</sup> A modern FTA usually has a series of chapters covering very similar grounds as the EU-China dialogues do, quite a few of which are initially moulded after the trade areas covered by the various WTO agreements China acceded to. In addition, it is good to remember that in 2014 and 2015 the EU-China summit declared the willingness to envisage a deep and comprehensive FTA as a longer-term perspective when conditions are right. This might be read as a judgment that the dialogues can support a good deal of the technical preparation of such a major undertaking. On the other hand, the number of EU-China dialogues has increased, organically, over the years – reflecting the closer bilateral relations over a broad spectrum of policy areas.

However, this view suffers from two severe shortcomings. Dialogues are too often uncoordinated, even when properly within the competence of respective EU institutions. They are also frequently ‘bottom-up’, unlike in an FTA strategy. At the same time, the modern EU FTAs nowadays are ‘deep and comprehensive’, which means that a good deal of their substance is ‘regulatory’. It so happens that most issues in the trade-related dialogues are regulatory in nature, too, simply because a good deal of the initial architecture of dialogues was modelled after the various subject matters of WTO agreements and – later – the intended Partnership and Cooperation Agreement. What is difficult to assess from afar (and from what is publicly known) is whether and how much today’s regulatory EU-China dialogues are actually capable of improving EU companies’ market access for goods and services in China (see also 5.2 below).

<sup>34</sup> The text says “[a]fter the issue has been raised by the EU in different bilateral meetings”, which are most likely to be one or more dialogues. Unfortunately, in the 2019 report, no efforts traceable to dialogues can be found, although China is prominent in the report. Cf [www.trade.ec.europa.eu/doclib/docs/2020/june/tradoc\\_158789.pdf](http://www.trade.ec.europa.eu/doclib/docs/2020/june/tradoc_158789.pdf).

<sup>35</sup> Such partnership and cooperation agreements can be stand-alone agreements with EU partner countries but are also frequently a side pillar to an FTA concluded between the EU and the trading partner. In the case of China, the idea was to have no fewer than 22 chapters, many of which would cover aspects of trade relations that can routinely be found in EU FTAs.

<sup>36</sup> There is one example of FTAs concluded without a formal treaty, by the Association of Southeast Asian Nations (ASEAN). ASEAN is itself an FTA and therefore has no common trade policy. Nevertheless, it managed to conclude (umbrella) FTAs with Japan, China, Korea and some other partners, underpinned by official FTAs on a country-by-country basis. The EU and ASEAN have expressed a preference to (eventually) conclude an FTA, which would somehow be underpinned by EU FTAs with most ASEAN countries.

Therefore, we are unsure but rather doubtful about whether the web of dialogues serves as an unbundled or fragmented FTA piece-by-piece, without a treaty.

### 5.3 Can the dialogues stimulate ‘sustainable development’?

The short answer is that they do, ever since 1994 for energy and shortly thereafter for the environment, and subsequently for labour and the climate. In other words, as sustainable development is a very important and comprehensive non-trade policy objective, EU trade policy in a wider sense exerts a positive influence on such objectives in China.

The overriding rationale for this ‘effectiveness’ is found in the gradual process of convergence of China and the EU’s strategic *objectives* in this enormous domain. Chinese policy preferences and objectives gradually converging with the EU ones has made China susceptible and actively interested in constructive debates on reforms, mimicking the EU’s best practices where possible. For the same reason, China has been keen to participate in a host of practical and administrative programmes related to aspects of sustainable development. There are essentially four areas that, together, make up sustainable development and China has shown active interest in all four. China has improved its occupational health and safety laws (there is an EU-China dialogue on this topic). In terms of labour rights (sometimes referred to as international labour standards),<sup>37</sup> China today adheres to six out of eight core conventions of the International Labour Organization (ILO) (not those on freedom of association or on collective bargaining). It has also improved and tightened over time its environmental laws and enforcement, for instance on chemical pollution as well as other air quality issues,<sup>38</sup> landfill issues, soil protection (with EU member states), waste treatment, upgraded water quality and e.g. plastics. China has been involved in climate issues for decades and ratified the Kyoto protocol (but assumed modest obligations at first as a – then – developing country). The 2015 Paris Agreement was of course a truly global effort, but China and the EU have been working closely together to achieve this significant result.

Two RESPECT papers on dialogues between the EU and China on sustainable development are forthcoming: one on labour and related social questions (Hu & Pelkmans, 2020), and one on environmental and climate policies (Pelkmans, 2020) for which the bilateral cooperation on sustainable forestry and timber trade is highlighted in Box 6. The former includes an analysis of the convergence of occupational health & safety over time through dialogues and related programmes, as well as China’s adherence to ILO core conventions and the policy ideas behind it, including the ILO decent work agenda. In addition, there will be a lengthy analysis of social protection in China in the period around 1995 until 2020. The latter paper surveys the process

<sup>37</sup> Although these are regulations once incorporated into national law rather than standards, which are by definition voluntary.

<sup>38</sup> It took China a long time before it finally began to force SO<sub>2</sub> emissions downward (high SO<sub>2</sub> emissions caused a lot of hardship and disease, as well as acid rain in and beyond China). However, here China did not follow the EU example of restricting these emissions at source – capping the use of coal severely, for example. China kept on increasing coal use and installed end-of-pipe technology (desulphurisation filters), which has limited potential.

of convergence in the fields of the environment and climate, with detailed attention on the starting position of China in the mid-1990s, when its growth was pursued 'at all costs', followed by a careful inspection of policy developments and indicators with respect to the environment and climate mitigation until 2020.

*Box 6. EU-China cooperation on sustainable forestry and timber trade*

The EU is a net importer of wood, certainly tropical hardwood. It has long been promoting sustainable forestry for tropical woods, for environmental and climate reasons but also for ensuring a reliable international framework enabling the import of sustainability-certified hardwood into the EU. This is the motive of the EU FLEGT<sup>39</sup> initiative concluded with several ASEAN countries as well as some African ones. China is the largest wood importer from ASEAN and increasingly from Africa as well. The 2009 bilateral cooperation mechanism with China on FLEG initially focused on China's own laws (given its 1998 restrictions on harvesting wood domestically and the tightening later) and practices but quickly widened to encompass the trading aspects as well. Using FLEGT in Indonesia (the leading FLEGT country) or ASEAN at large is probably pointless without involving China as the biggest importer. China's huge timber & pulp imports in 2017 amounted to \$51 bn; it used to be a formidable exporter as well but it has lost a third of its sales abroad since 2007. In 2019, there were 15 FLEGT voluntary partnership agreement (VPA) countries that have minimum regulation and certification requirements as a condition for exporting to the EU. This has acted as a standard for quite a few countries and stimulated China to act in a similar fashion. How important this all is can be seen if one knows that Chinese timber imports from FLEGT VPA countries between 2007 and 2017 increased by 136% in US\$ value. On the export side, some 52% of Chinese exports of timber products were bound for regulated markets, i.e. only demonstrably legal timber can be imported.

During the 9<sup>th</sup> meeting of the Bilateral Coordination Mechanism in March 2018, a workplan was adopted with a host of issues or options to address this question, such as import-management structures, the development of the Chinese Timber Legality Verification System, a new monitoring system with guidelines and more incentives for the private sector to adopt responsible purchasing of forestry products. Meanwhile, China has amended its forestry law in 2020 prohibiting the purchase, transport and processing of illegal wood. The EU, China and Indonesia have developed a dialogue with respect to FLEGT and VPAs, whereas Vietnam-China and Myanmar-China talks have begun (inspired by FLEGT and stimulated by the EU). Such a dialogue is also undertaken with China and Africa.

<sup>39</sup> FLEG stands for forest law enforcement and governance. With the trade component in, it becomes FLEGT.

For present purposes we limit ourselves to illustrations of the recent dialogue process and substance. Current dialogue work on energy is based on the China-EU Roadmap on Energy Cooperation for 2016-20.<sup>40</sup> This roadmap goes surprisingly far, even including harmonisation. On energy supply, it seeks to reduce costs by ‘improving competition’ via trade and investment. This intriguing policy intention between the EU and China ought to be investigated empirically now that the four-year Roadmap is over.<sup>41</sup> On energy demand and efficiency, the Roadmap is ambitious. It suggests mutual recognition of existing and future schemes, harmonising energy labels and going for market-oriented energy-performance contracting. Again, this asks for further research and clarification.

On cross-cutting issues, three aspects seem equally ambitious. First, the Roadmap speaks of harmonising regulatory ‘grid’ policies, which seems very ambitious indeed. Second, the partners advocate the promotion of markets for ‘green goods’. Here, as a member of the Asia-Pacific Economic Cooperation (APEC), China has supported a ‘green goods’ plurilateral agreement in the WTO (a follow-up of APEC’s green goods arrangement) and so has the EU but these negotiations are currently stuck.<sup>42</sup> Promoting domestic markets for green goods might be a reason for mutual emulation but this would need to be analysed further. Third, and somewhat surprisingly, the roadmap seeks cooperation within the framework of the Energy Charter, so far a legal framework with EU-like rules for a much wider European area. The (economic and trade) meaning of this intention and the possible link with the Belt and Road Initiative will have to be addressed in further work. One possible, suggested reason behind this close cooperation is the long-run strategy of the large electricity companies in China (the largest in the world and all SOEs) vis-à-vis Europe, envisaging takeovers and tighter connectivity between the two electricity systems.

The joint EU-China political leaders’ declaration in Beijing<sup>43</sup> of 2018 suggests further deepening relations on climate change and clean energy. In the declaration, and confirming an earlier point, the partners step up their bilateral cooperation for implementing the Paris Agreement, including the international cooperation to this effect. It also enhances technical, economic and scientific cooperation while explicitly involving the European Investment Bank. Leaders reaffirm their strong commitment to the \$100 bn climate fund for developing countries and new funding after 2025. They express support for the Kigali amendment (of the Montreal treaty on hydrofluorocarbons) and pledge to jointly phase out harmful heating, fridges and air-conditioning liquids. Finally, China is now unambiguously committed to lowering emissions in air and maritime transport, which has long been a controversial issue.

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<sup>40</sup> See the “EU-China Roadmap on energy cooperation (2016-2020)”, European Union and Government of the PRC ([https://ec.europa.eu/energy/sites/ener/files/documents/FINAL\\_EU\\_CHINA\\_ENERGY\\_ROADMAP\\_EN.pdf](https://ec.europa.eu/energy/sites/ener/files/documents/FINAL_EU_CHINA_ENERGY_ROADMAP_EN.pdf)).

<sup>41</sup> Note that the roadmap also includes a range of highly specific items on supply.

<sup>42</sup> See de Melo & Solleder (2019) for a detailed analysis of the complications of the green goods plurilateral.

<sup>43</sup> See the “EU-China leaders’ statement on climate change and clean energy”, Beijing, 16 July 2018 ([https://ec.europa.eu/clima/files/news/20180713\\_statement\\_en.pdf](https://ec.europa.eu/clima/files/news/20180713_statement_en.pdf)).

With respect to the social pillar of sustainable development, the employment and social policies dialogue began in 2005. A major technical project<sup>44</sup> through which China wanted to acquire knowledge and tap the experiences of EU member states (social security is not an EU competence) began in 2006 for four years, and this project was undertaken by the Chinese administration in Beijing. The dialogue on occupational health and safety was initiated in 2009, soon followed by a special project on this topic in high-risk sectors. Starting in 2014, the EU-China project on social protection reform ran to 2019, with a follow-up – together with the ILO – on “Improving China’s institutional capacity towards universal social protection” until 2022. Under the 2013-20 EU-China strategic agenda for cooperation, the part on ‘social progress’ indicates a series of initiatives connected to social protection and cohesion.

This short description of EU-China dialogues and programmes on sustainable development makes it very clear that i) the gradual convergence is real and goes quite far; and ii) it has led to concrete and significant policy implications for both economies as well as for international cooperation. Since sustainable development has become a major trade and investment issue, these policy commitments support the premise that non-trade policy objectives can be and are supported by the EU’s trade and investment policy, and, in this area, to amazing degrees. However, one has to assess this conclusion properly, because it hinges on two critical aspects: the gradual convergence over time of the objectives of the two partners, and a rather long period (here, some 25 years) in order to avoid studying merely a few ‘trees’ of the forest and the risk, as well, of missing out on China’s long-run approaches.

It is at least doubtful whether the long-run rapprochement in climate and environmental policies, and to a considerable extent also in social protection and most of the labour standards, would have gone so far, had the overall long-run objectives not been converging over time. It can therefore be maintained that the relative effectiveness of these specific dialogues over decades is a function of the more fundamental process of convergence in these two pillars of sustainable development. Farnell & Crookes (2016) are more sceptical for the majority of dialogues, without specifying them in this quote:

While the broad scope of discussion may be defined, there is often no specific goal, except to contribute to mutual understanding... In most cases, there is no oversight of the discussions at the political level, no timetable for results and no sense of urgency to make progress.

This sweeping statement is surely much too general as we show for the environment and climate as well as for the (generally more sensitive) social pillar of sustainable development. Although Farnell & Crookes (*op. cit.*), acknowledge ‘practical objectives’ in some policy areas and provide a few precise examples<sup>45</sup> as well as a short overview of considerable funding for articulated programmes, their view is that these are the exceptions. Following a few case studies on energy, the environment, climate and urbanisation (often linked to those), their

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<sup>44</sup> The EU-China social security reform cooperation project.

<sup>45</sup> Such as on standards for electric vehicles and specific issues in customs procedures.

conclusions are sombre. That is not to say that little seems to happen; extensive networking occurs, but cooperation is rarely ‘deep’ and mutual. “In general, ... the exchanges are limited to government officials ... hardly business, and when it does the result has been judged insufficient by the European side”(p. 187). Influence on policy “is one-way, from the EU to China... .The benefits of EU-China cooperation for the real economy ... appear to be very limited” (p. 188).

It is good to be warned by Farnell & Crookes not to read too much in frantic dialogue activities and networking. But there is substantial evidence that more than two decades have not been without explicit and tangible rapprochement in, e.g. climate mitigation and the environment. That notwithstanding, in China there is often a long period from public announcements to concrete policy implementation and that is certainly the case with sustainable development. Moreover, Farnell & Crookes had finished their book just before the Paris Agreement on Climate Change and before the enactment of the three paramount and much firmer environmental laws on air, soil and water in China (with respect to 2015, 2016 and 2018, see Pelkmans (2020) for detail). Additionally, in the social field it can be shown that China has looked to the EU for inspiration and experience, with the EU eager to witness social progress in China. There are also signs that the time horizon of Farnell & Crookes might be too short, something that we have attempted to avoid to the extent feasible by covering up to 25 years of the cooperation.

#### 5.4 Can dialogues address ‘systemic’ differences’?

China boasts about its ‘socialist market economy with Chinese characteristics’. When the EU and China look back on some 25 years of bilateral dialogues on market orientation, market opening for trade and investment, various forms of close cooperation and many aspects of reforms in China, an inevitable query comes up: should the focus on numerous ‘trees’ (i.e. the many dialogues) be preceded by a well-founded view of the ‘forest’ (what about the Chinese system of a socialist market economy underlying many bilateral policy issues and, indeed, many problems in the WTO)? A significant and complicating factor is that neither China nor any other country with a ‘socialist’ ideology<sup>46</sup> is a democracy with recognised and legally protected freedom of speech and information (or indeed research) – that is, open, well-informed and unrestricted debate – as well as social and political rights of association. This mere fact renders it a priori most unlikely that fundamental systemic differences can be fruitfully discussed in earnest, even when diplomatic accommodation in informal and closed settings might take place.

From the literature it is clear that, several decades ago, many countries or leading politicians in several parts of the world might have entertained expectations of a gradual change of China’s socialist market economy, in which case the EU (as well as the US, separately) also had a cooperation programme on governance for village suffrage, for example, with some of them

<sup>46</sup> Take Vietnam, Cuba and North Korea, for example.

believing in an eventual shift to a multiparty system with greater social and political freedoms. By now, these expectations and erstwhile beliefs have been eroded if not eliminated. If this is correct, the query becomes whether informal but frank and fact-based discussions in bilateral dialogues can address systemic differences of socio-political tenets underlying the socialist market economy. The short answer is no. Such initiatives would be regarded, inevitably, as attempts at regime change and hence be taboo. Diplomatic parlance would have it that this would be an unacceptable interference in domestic affairs. It would furthermore undermine the spirit of the strategic partnership currently upheld firmly by China and the EU, despite occasional frictions. Some in China even suggest informally that the EU would resist, equally categorically, any attempts by China to discuss a reversal of democracy and of a relatively non-interventionist economy, even though China's doctrine has it that democracies exhibit fundamental weaknesses and markets require far more steering by direct government instruments, including a major role for SOEs.

In this respect, it is worth quoting the work of Max Roger Taylor (2019), another rare book<sup>47</sup> in which numerous interviews with officials involved in EU-China cooperation lay at the basis of the conclusions. For present purposes, when addressing systemic trade issues derived from the socialist market economy with Chinese characteristics, his three negative<sup>48</sup> hypotheses about promoting EU values with China should be considered:

- a) Raising the most EU controversial values with China is expected to trigger an obstructive response by the Chinese side which will critically undermine dialogues.
- b) Value mainstreaming is pointless as well as risky, as Chinese interlocutors are perceived likely to be unable to meaningfully impact Chinese policy connected to EU controversial values.
- c) [There is a] perception among EU officials that China is not listening to [the] EU and it should.

All three hypotheses are frequently heard in conversations. They might as well apply to the discourse about the systemic trade issues of the socialist market economy with Chinese characteristics.

The fundamental query is therefore a derived one: can systemic differences be addressed in the framework of bilateral and multilateral trade and investment rules, and accepted world practices? The economic case for such actions must rest on the extent and gravity of distortions and the potential or actual negative spillovers engendered. What renders it so problematic is that 'extent and gravity' as well as negative cross-border spillover are far from easy to establish firmly. Many other countries intervene in multiple ways in their markets, which implies that it is a tall order to distinguish 'systemic' from other interventions. For the WTO it is known that,

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<sup>47</sup> It is a Ph.D. dissertation at the University of Bath.

<sup>48</sup> He also puts forward two positive hypotheses. See Taylor (2019, p. 280, table 10.1).

to some extent and for some forms of interventionism and controls, specific distortions can be addressed, whereas for other ‘distortions’ this is either doubtful, given the gaps and omissions in the rules and rulings of the Appellate Body, or as yet impossible. So far, the filing of WTO cases by both China and the EU (also outside the trade defence area) has not undermined the spirit of the strategic partnership.

Nineteen years after WTO accession, it is a fair judgment that China is (roughly) WTO compliant where legal texts in the WTO are clear and straightforward (see, e.g. Grieger, 2016, and the literature quoted). There are surely some outstanding compliance issues, and one particularly serious example is industrial subsidies.<sup>49</sup> About fisheries subsidies there is very little clarity. It would seem to be a different matter altogether where the implicit assumption (of original participants in the General Agreement on Tariffs and Trade and members of today’s WTO) that trading partners are market economies is less than properly incorporated in the written rules, or not at all, or where actual implementation or enforcement of accepted WTO disciplines is weak or literally failing. Even a relatively simple discipline such as careful and timely notification of, e.g. subsidies, in various forms has been followed up in lax ways or not at all in forms useful for trade policy. That is the case not only for China<sup>50</sup> but holds in particular for China because there are powerful indications that distortions occur and are aggravated because of its sheer size in the world economy. Recently, there has been much more explicit attention on such omissions and the de facto circumvention of what market economies typically regard as routine market disciplines. Moreover, there are non-trivial signals that under President Xi, the systemic differences have widened.

It is not publicly known how the EU-China dialogues at the top level have dealt with the forest of systemic differences relevant for trade and investment. What is known is that the EU has insisted that China should pursue a broad economic reform route for markets to work better, and that it supported the rich November 2013 Chinese Communist Party (CCP) reform plans as a manifestation of this approach. However, when it became clear that these reform plans turned out to be a paper tiger, the concerns of China’s trading partners including the EU increased exponentially, not least because China had meanwhile initiated radical and interventionist plans for many business sectors, with apparently massive funding in ingenious ways.

The present report is not the place to set out these concerns in analytical detail,<sup>51</sup> but the upshot has been a new China strategy for the EU since March 2019.<sup>52</sup> Dubbing it a ‘new’ strategy is not correct as the main elements have been adopted from the 2016 strategy, but there is no doubt that the wording and style are far more assertive than hitherto. This newly formulated strategy and several important WTO cases touching on some of the suspected

<sup>49</sup> See Hu (2019b) on industrial subsidies; see also the WTO’s “Trade Policy Review: China” (2018), at p. 17.

<sup>50</sup> However, just to select one prominent example, India has carefully complied with the obligations to report on subsidies in the WTO.

<sup>51</sup> See Pelkmans (2018) for an elaboration; see also EPSC (2019), Heilmann (2018) and Zenglein & Holzmann (2019) (<https://www.merics.org/en/papers-on-china/evolving-made-in-china-2025>).

<sup>52</sup> See EU-China – A strategic outlook, JOIN(2019) 5 final, Strasbourg, 12 March 2019, op. cit.

distortions at stake, not to speak of the U-turn of the US administration led by President Trump, have made China realise that it has to respond to these pressures by further opening up (be it selectively once again), accelerating the CAI talks by setting an end date and working together with the EU in a bilateral dialogue on WTO reform.<sup>53</sup>

The EU has also responded with the introduction of an EU framework of investment screening as a basis for possible restrictions for reasons of national security and public order (but a somewhat wider concept of security). This screening is more a ‘sign on the wall’ than a very restrictive tool but it is a credible signal that the EU has become vigilant about incoming FDI. The same approach applies to some EU member states, such as Germany. Also, the Commission’s 2020 white paper on foreign subsidies affecting economic activity in the EU single market reflects concerns about systemic issues vis-à-vis China, even when China is not singled out as such.

For the EU, the ‘socialist market economy with Chinese characteristics’ has certain tenets negatively affecting trade and investment in bilateral and multilateral ways:

- the many methods (often hidden or non-transparent) and sheer quantities of subsidies, including more than 1,700 heavily state-influenced investment funds;
- the steering and direct influence of the state on SOEs, and these SOEs are often giant firms, in sectoral markets dominated by them, and/or they largely control leading R&D subsidies and programmes (if not research institutes and laboratories) in what are called industries of the future. Unlike in the EU for example, SOEs are not embedded in an overall pro-market regime, with strict transparency rules about the financial relations between the state and the companies, along with prohibitions or conditioning of state aid;
- the ever-increasing direct role of the Party (CCP) in firms, and not only SOEs but also in more than 200,000 *private* Chinese companies. Usually, the CCP representative sits on the board; this phenomenon is unknown in any other WTO partner (as far as we know). There is nothing ‘Chinese’ about this characteristic – it is Party control for motives other than market-led ones. The newest target of this highly intrusive CCP attempt to control or steer companies in what is supposed to be a market economy are foreign enterprises in China. This began in 2017, in particular for joint ventures of foreign enterprises with local SOEs. In September 2020, however, a much broader approach has been assumed by the CCP, applying to foreign firms as well, which has raised serious concerns with the foreign business community in China;<sup>54</sup>

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<sup>53</sup> Of course, concluding the Phase 1 Economic and Trade Agreement with the US (January 2020) is another step taken by China to open up.

<sup>54</sup> See the press release of the European Chamber dated 12 October 2020 (<https://european-chamber.com/en/press-releases/3291/european-chamber-stance-on-united-front-work-in-china-s-private-sector>). Among

- condoned or forced technology transfer when a foreign company wants to invest in China. Given the enormous market size of China, also rapidly growing, this ‘soft’ instrument can be quite effective, because the only alternative for firms is to quit China, which is often even less attractive;
- widespread restrictions on incoming FDI and often highly discretionary treatment (under licensing regimes) rather than mere general rules. China also steers or even controls *outward* FDI, which – for a country with huge foreign exchange reserves – cannot be explained by balance of payment considerations; managing outward FDI is alien to a market economy; and
- a number of dubious or unusual interventions that China maintains in goods trade, including VAT exemptions and a battery of export restrictions.

That said, a socialist market economy with Chinese characteristics per se need not be a problem for market access. A ‘marriage of convenience’ no doubt, China innovatively coined the term to accommodate two opposing ideologies, i.e. the legitimacy of one-party Communism in the country and a market-driven model of development with private property rights, in order to qualify for membership at the WTO, which is in effect only for market economies. The principal issue with the socialist market economy with Chinese characteristics is the Chinese government’s continued role in influencing the markets, which is also incompatible with its WTO commitments.<sup>55</sup> Practically all these issues can be addressed in EU-China dialogues but there seems to be little public information on whether they are and whether that leads to fewer interventions. One effect recently is that systemic differences are widely debated in many capitals in the world, not least in Geneva and Brussels. Unfortunately, the EU-China WTO reform working group has not published its deliberations.

## 6. Conclusions

EU-China dialogues fulfil many useful functions and a large majority of some 50 or so of these dialogues is directly or indirectly relevant for trade and investment. Today’s architecture of the EU-China dialogues can be traced back to the following rationales:

- early development needs and requests for policy learning, which China (and international organisations) expressed decades ago;
- some first dialogues linked to the 1985 EU-China non-preferential trade agreement;
- preparation for China’s accession to the WTO – when the EU offered capacity building and support programmes, with in-depth exchanges in the many areas of the WTO; and

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the 28 clauses in the opinions, a striking one is clause no. 8, where it says that the CCP seeks to develop “a backbone of private businesspeople that can be relied on at critical moments”. This statement is a plain distortion in and by itself because CCP allegiance, instead of market principles and incentives, matters most.

<sup>55</sup> See Hu (2019b) on industrial subsidies; see also Hu (2019a) on China as a WTO developing member.

- iv) the persistent urge on both sides for China to reform deeply and structurally as China migrated out of the top-down and rigidly planned economy (without much private economic initiative allowed) towards a market economy.

Today, the underlying rationale for having so many trade-relevant dialogues is that modern trade and investment policy covers a very broad spectrum of policy areas. Moreover, there are permanent and emerging issues to address jointly in the world economy and at the same time new opportunities to enhance job growth via increased trade and direct investment. This wide range is also reflected in the proliferation of WTO agreements and new<sup>56</sup> areas of attention.

Within the EU, the recent assignment of a wide range of areas to EU trade policy, instead of the member states being competent, has certainly caused a further expansion of the scope of EU-China dialogues. This widening of the scope of EU-level trade policy began with the 1991 opinion of the Court of Justice of the European Union, followed by its 2017 opinion on the legality of several aspects of the EU-Singapore FTA.<sup>57</sup> A comparable widening of scope has been found in FTAs concluded<sup>58</sup> by the EU and by several other OECD countries with both developed and developing countries. An important underlying reason for this broadening is ‘trading costs’ – the effective cost differential between bringing goods to the domestic and to a foreign market (apart from transport and insurance, which are inevitable).

In the case of China, as mentioned above, the proliferation of dialogues has several explanations. In short, among them is the demand for wide-ranging consultation and mutual policy learning given the lack of an FTA for such an important trade and investment relationship, and (initially) the developmental and support needs of China in a series of technical fields. Most prominently is the powerful quest for socioeconomic and market reforms, which is expected to have a positive impact on market access as well as on the better functioning of the Chinese market (including a level playing field for foreign enterprises).

The following conclusions on the role and functions of dialogues under the EU-China comprehensive and strategic partnership are based on a data search (Hu, 2020), which is unfortunately incomplete as the reporting on EU-China dialogues by the two sides is neither centralised nor systematic, but scattered and very incomplete. Nevertheless, we believe the survey of the data is the best available so far.

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<sup>56</sup> Although some are not so much new as better accepted in the global trade community (cf. the four so-called Singapore issues going back to EU proposals in 1996).

<sup>57</sup> Opinion 2/15 declares that the EU’s exclusive competence in trade does not cover just two aspects, namely the field of non-direct foreign investment (‘portfolio’ investments made without any intention to influence the management and control of an undertaking) and the regime governing dispute settlement between investors and states.

<sup>58</sup> In the case of Mexico, the FTA concluded in the late 1990s even had to be *upgraded* recently so as to accommodate the policy demand for widening the scope and deepening of commitments.

We asked four specific questions, after first mapping the EU-China dialogues.

1) *Do dialogues improve market access?*

Dialogues would seem to have facilitated market access in a variety of ways: helping Chinese laws to align with WTO laws, supporting the delivery of specific WTO commitments, strengthening enforcement by China (including technical controls), stimulating its opening-up in specific fields (like air transport and maritime) and assisting China to level the playing field internally, which is also helpful for EU companies in China.

However, when it comes to classic tariff setting, China is unilateral (under bound tariffs). In trade defence there have been two dialogues (one on trade defence instrument (TDI) best practices and one on market economy status), but the EU has only further increased its TDI restrictions vis-à-vis China. Thus, these two dialogues might have accomplished little more than letting off steam by complaining.

The EU has also consistently insisted on reforms in China with a view to easing restrictions that hinder effective market access. On some aspects, this seems to have worked but not on the big issue of SOEs and their privileges. We show that SOEs under President Xi have rapidly gained prominence and support, even at the expense of private firms. Moreover, the factual application of the Anti-Monopoly Law (inspired by EU law) to SOEs, and in particular to mergers between large SOEs, is plainly anticompetitive. Market access and post-establishment liberalisation for EU FDI under 'national treatment' is a key subject of the Comprehensive Agreement on Investment and is of course a negotiation for a treaty, not a dialogue matter. On forced technology transfer, dialogues failed to work and the EU eventually settled for filing a WTO case, similar to the US and Japan. On intellectual property rights, however, dialogues and follow-up programmes have been quite successful – the remaining (serious) problem is enforcement. For geographical indications, a seven-year negotiation resulted in an EU-China agreement in 2019, with 100 GIs on both sides to begin with. On technical standardisation, the partners still have a dialogue on technical barriers to trade, along with a cooperation initiative that has been launched among three European standardisation bodies, based in Beijing.

Finally, since reporting of these dialogues is always couched in diplomatic language, we attempted to find traces in EU reports confirming these uses of dialogues. This led to a few revealing quotes on how dialogues matter in this respect and an admission that dialogues might often be more practical and less controversial than a legalistic approach in the framework of an FTA.

2) *Can the web of dialogues be seen as an unbundled FTA?*

The answer is not really. An FTA is no longer a short-run objective for either partner and the EU's two prerequisites for starting FTA talks have not been fulfilled: concluding the CAI and deep reforms in China (bound to include a different approach to SOEs). Building up an unbundled FTA through numerous dialogues on areas nowadays often included in deep and comprehensive FTAs requires refined coordination on both sides and this is absent. A lot of dialogues are bottom-up, fairly loose and non-committal, and basically not coordinated horizontally. Their links with the annual summit are usually 'vertical' by pleading the importance of the initiative or the field, not so much by the overall longer-term frameworks. The trade dialogues do not seem to substitute, even imperfectly, for an FTA, though the dialogue subjects coincide with a number of typical FTA chapters. Indeed, an eventual future FTA may be – in part – conveniently drafted based on some of the dialogues.

3) *Can the dialogues stimulate sustainable development?*

In sustainable development (including adherence to six of the eight ILO core conventions, though the last two are the most crucial), a considerable degree of recent convergence of EU and Chinese objectives has been extremely helpful for effective bilateral cooperation for both the social dialogues (labour standards and social protection) and the environmental & climate dialogues. The EU and China have worked together for two or more decades on a myriad of projects, programmes, dialogues, declarations (also through the summits) and via special funding. Thus, in recent energy cooperation the bilateral collaboration goes remarkably far, including even harmonising in selected areas. In climate strategies the EU and China have recently come to work closely together, but also did so in the heyday of the Clean Development Mechanism. On other aspects of the environment, after a history of dreadful neglect and indifference in China, with adverse public health consequences as well, the partners have cooperated in a number of different ways to achieve results, such as better (for instance, risk-based) regulation and more effective enforcement. The non-trade policy objectives under sustainable development have been supported actively by the EU, with continued interest from China, and occasionally with cooperation on the ground in China (e.g. with the cap-and-trade system).

4) *Can dialogues reconcile or at least mitigate 'systemic' differences?*

In the case of systemic differences, dialogues have not proven to be very useful in terms of results, if indeed this can be expected at all from dialogues. It is an accomplishment to keep channels of debate and exchange open. From the EU end, dealing with systemic differences effectively when the partner country takes pride in enjoying a socialist market economy with Chinese characteristics is intrinsically impossible. This question is so fundamental, if not existential given the overwhelming

and highly intrusive role of the CCP, that one can only hope to work on the incompatibilities with the WTO and the experienced negative spill overs from the massive interventionism in China. Dialogues here have been concrete on some issues (e.g. steel and the Global Forum on Steel; innovation in light of the China manufacturing 2025 programme) and ever-more firmly linked with WTO reform (indeed, a bilateral dialogue on this theme is ongoing), while at the same time WTO cases have been filed or joined by the EU. These features are reflected in the EU's China strategy of March 2019, in which China is regarded as a partner and a competitor, as well as a rival.

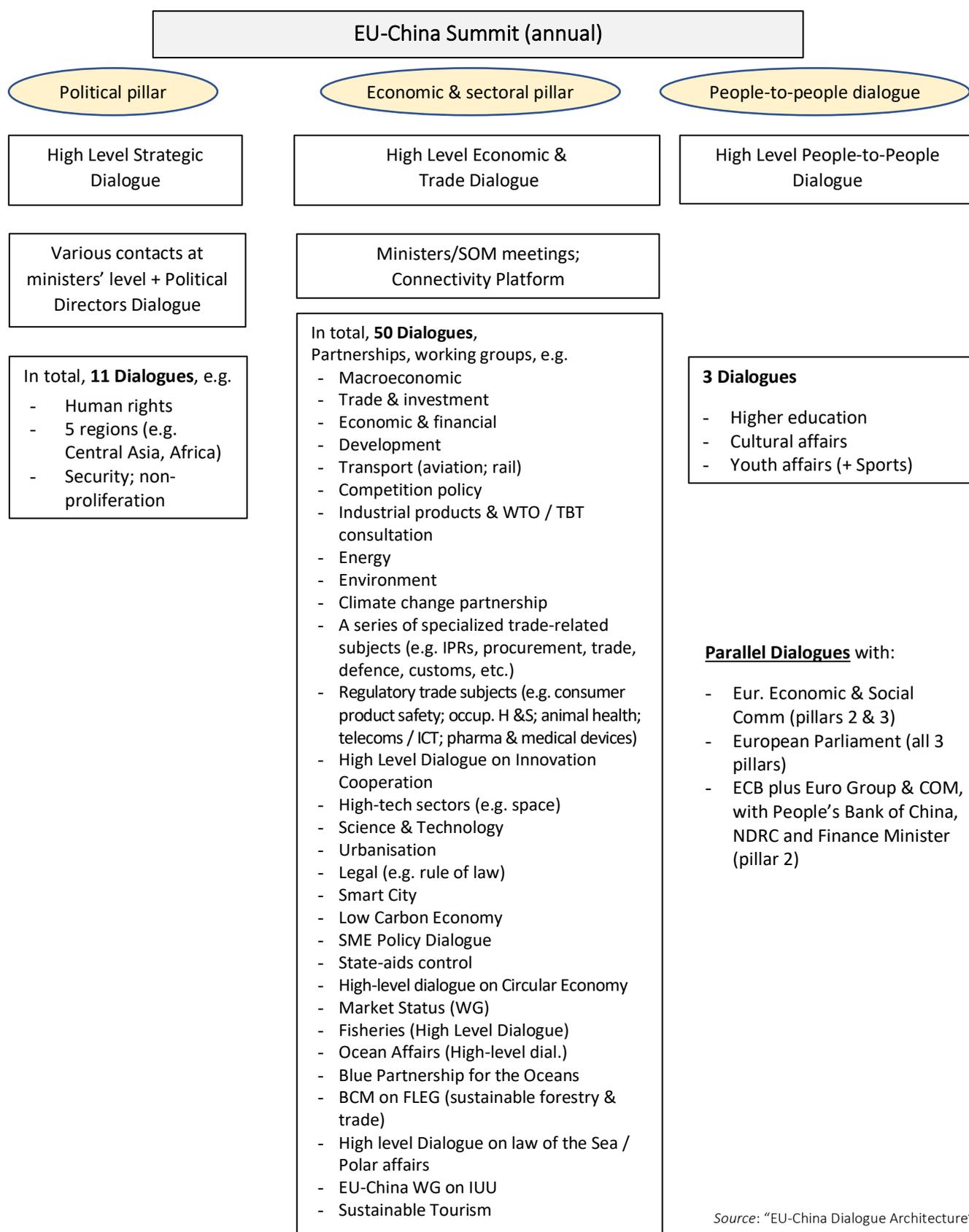
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## Annex. EU-China dialogue architecture and hierarchy

## EU-China Dialogue Architecture &amp; Hierarchy



Source: "EU-China Dialogue Architecture", European External Action Service, November (2015) and authors' compilation.



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