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An uphill struggle? Towards coordinated EU engagement with China's Belt and Road Initiative

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China's 19th Party Congress unexpectedly amended the party's constitution with a pledge to "pursue the Belt and Road Initiative". This further elevates the status of president Xi's heavily promoted foreign policy, which aims at creating trade and investment opportunities through the development of Eurasia's continental and maritime infrastructure. As the implications of this policy are increasingly felt across Europe, following years of growing Chinese investments, so are the challenges it presents to Europe's unity, prosperity and security. In light of these challenges a constructive engagement with China's Belt and Road Initiative (BRI) constitutes an immense task for the European Union, whose position has been weakened by growing dissent among member states over the Union's policy towards China.

INTRODUCTION

At its 19th Party Congress, the ruling Communist Party of China included a commitment in its constitution to follow "the principle of achieved shared growth through discussion and collaboration, and pursuing the Belt and Road Initiative".[1] The statement, which elevates the status of Xi Jinping's signature foreign policy, underlined the current president's expanding power while emphasizing the initiative's significance beyond Xi's presidential term. The Belt and Road Initiative (BRI), a vast programme to revitalize ancient trade routes between Asia, Africa and Europe through heavy investments in continental and maritime infrastructure projects, in other words, is here to stay.

The party's unwavering dedication to the BRI will undoubtedly affect China's relations with Europe, where the implications of growing Chinese infrastructure investments are increasingly felt. While initially viewed as a welcome support to Europe's debt-ridden South and underdeveloped East, recent statements by the EU and its larger member states primarily stress the challenges which the BRI presents for Europe's unity, prosperity and security.[2] This change in stance comes as no surprise. The BRI, as the first two sections of our briefing suggest, has yet to live up to its promise of being an inclusive, multilateral and sustainable 'win-win' project from which all parties stand to gain. Most concerning from a European perspective is the persistent absence of a level-playing field in investment relations as well as China's growing influence over individual member states, which increasingly hamper the EU's ability to deal with China collectively.

Considering the latter, our third section argues that the EU's ambition to constructively engage with China's BRI constitutes an increasingly daunting task as dissent among member states over the Union's China policy continues to rise. This is not to say that the EU is incapable of shaping China's initiative. The EU's market size, Chinese investment interests and the BRI's pressure to succeed all strengthen the EU's position to negotiate a BRI that works for all. Doing so, however, will require a strong and creative effort to unite member states behind a clear and robust European position.

AN INCLUSIVE, MULTILATERAL AND SUSTAINABLE INITIATIVE? THE BRI IN THEORY AND PRACTICE

When addressing delegates at the first Belt and Road Forum in May, Chinese president Xi Jinping did not fail to emphasize BRI's cooperative and inclusive character.[3] The initiative, as Cui Tiankai, China's ambassador in Washington, had put it, would not be a 'solo show' but rather a symphony performed by all participating countries.[4] The Belt and Road forum held in Beijing, a spectacle attended by delegations from 130 states and international organizations, served to prove this point.

The event, moreover, is not the only testimony of BRI's multilateral aspirations. Chinese efforts to enhance the initiative's cooperative image, for instance, reflect in the establishment of the Asian Infrastructure Investment Bank (AIIB), a multilateral development bank, which started operations in 2016. The AIIB, while not directly linked to the BRI, assists the initiative's implementation by providing loans for related infrastructure projects. A British government decision in 2015 to defy US pressure and join the Chinese-led institution was a crucial moment in strengthening the bank's multilateral character as it triggered a wave of accessions by European as well as regional economies, including South Korea and Australia.[5] European states, and the UK in particular, played an important part in strengthening the multilateral image of both the AIIB, and by extension China's Belt and Road Initiative.

This multilateral image, however, quickly fades at a second glance. The AIIB, despite its increasingly diverse membership, continues to be firmly controlled by China, which maintains a de-facto veto on substantial board decisions (taken by a 75% supermajority). The gap between China's voting share (27.5%) and that of second-ranked India (7.9%) furthermore constitutes the largest in any multilateral development bank.[6] Moreover, it is important to note that the AIIB's multilateral character stands out within the network of institutions, which finance BRI-related infrastructure investments. Within this network, state-owned institutions, above all the Silk Road Fund, the China Development Bank (CDB), the Export-Import Bank of China (Exim) and China's state-owned commercial banks currently set the tone while the AIIB only constitutes a minor component.[7] Xi's recent pledge to invest an extra $14,5bn into the Silk Road Fund and launch a $43.5bn lending scheme operated by CDB and Exim, furthermore underscores China's intent to maintain control over the finance and implementation of its envisioned Belt and Road.[8]

In turn, this finance structure diminishes hopes for a multilateral regulation of implementation and operation standards. Environmental or transparency standards agreed in the AIIB, in which Europeans have a seat at the table, cannot guarantee their application in BRI projects financed by other institutions. At the same time, recent European experiences with Chinese infrastructure investments indicate that high transparency and sustainability standards, and their consistent application, cannot be taken for granted. Chinese investments in a rail link between Budapest and Belgrade, a BRI showcase project in Europe, are currently under investigation for their compliance with EU public procurement law.[9] In another case, the construction of a Polish highway by a Chinese state-owned contractor led to price-dumping allegations and the contract's eventual cancellation following the provider's financial difficulties.[10] Chinese investments in the construction and renovation of thermal power plants in Serbia and Bosnia moreover raised environmental objections and questioned BRI's aspiration to provide sustainable and environmental friendly solutions.[11] Considering these experiences, it comes as no surprise that Europeans have become increasingly concerned with the BRI's commitment to social, environmental and transparency standards. At the Belt and Road Forum in May, these concerns led Europeans to snub Xi Jinping by refusing to sign a trade document for its lacking commitment to transparency and sustainability standards.[12]

Is the BRI a win-win project?

Alongside promising an inclusive, multilateral and sustainable initiative, a catchphrase in the promotion of BRI has been its potential to provide 'win-win cooperation'. Infrastructure investments, the argument goes, would create trade and investment opportunities from which all parties stand to gain. While this notion is persuasive, a closer look at the present impact of BRI-related investments in Europe gives reasons to doubt whether these have left Europeans better off.

The EU's trade balance with China has been consistently negative for the past decade, reaching a record low of -€180bn (trade in goods) in 2015.[13] Improved infrastructure links and falling transportation costs stand to disproportionately benefit China. A pilot container train on the Yiwu-Riga route, an overland rail link, illustrates the potential effect. Since being put on rails, the train has mainly run in one direction: from China to Europe.[14]

Growing Chinese investments in Europe's infrastructure and high-tech sectors moreover leave Europeans increasingly worried about persistent trade and investment barriers. In 2016, Chinese investments in the EU increased by 77%.[15] In the same period, EU investment in China declined by a quarter.[16] The European Chamber of Commerce in this light warned about a persistent lack in reciprocity, noting that many of China's investments, such as Midea's takeover of Kuka, a German robotics maker, would be unimaginable investments for European companies in China.[17] This warning has been echoed by the European Commission, which, following a string of Chinese investments in sensitive European assets, including utilities, transportation infrastructure and technology identified the establishment of reciprocity as a pressing challenge.[18]

Large-scale Chinese investment in Europe's infrastructure, moreover, does not only bring about economic challenges. Worries are also directed at China's growing political clout in Europe, which might increasingly enable China to neutralize the EU's stance on contentious issues by wheedling individual member states into blocking joint EU statements and initiatives. For instance, in June Greece blocked an EU statement prepared for the scheduled review of China's human rights situation in the UN Human Rights Council. Following a foreign ministry spokesperson, Athens rejected the statement on the grounds of providing 'unproductive criticism'.[19] It was the first time that the EU was unable to formulate a joint opinion for the review of an individual country at the UNHRC.

On another occasion, Hungary and Greece, both major recipients of Chinese infrastructure investments, pressed the EU into toning down its reaction to a ruling by the permanent court of arbitration (PCA) issued in July 2016, which sought to settle a maritime dispute between the Philippines and China over the legal basis for Chinese claims to 'historical rights' to resources in the South China Sea. When China rejected the Court's decision as 'naturally null and void' the EU reacted with an uninspired acknowledgement of the ruling rather than the appeal to international law many had hoped for.[20] Both events have since given rise to concerns that China's rising political clout would erode the EU's ability to perform its role as an upholder of human rights and an international rule of law.

MOVING FORWARD: HOW EUROPEANS SEEK TO SHAPE BRI'S FUTURE

Following the increasingly salient implications of Chinese investments in Europe's infrastructure, EU member states and institutions have become eager to identify suitable responses. One reaction has been a push to strengthen European coordination in the AIIB. As members of the institution, Europeans hold around 20% of the votes in the bank's executive board; nearly enough to block substantial decisions taken by supermajority (75%). Vote coordination and cooperation with like-minded partners, such as Australia (3.6%) and South Korea (3.7%), thus presents a potential tool for Europeans to exert influence over the standards that the AIIB applies in financing BRI-related projects.[21] At the same time, vote coordination in the AIIB gives Europeans only limited influence over the implementation of China's Belt and Road initiative as the AIIB, at least so far, only finances a fraction of BRI-related investments. To shape the implementation of China's Belt and Road initiative, other measures are therefore necessary.

In response to this, the European Commission suggested the establishment of a European mechanism for screening foreign investments in strategic assets, which include critical technologies, infrastructure, inputs or sensitive information.[22] This measure, the Commission argued, would enable the Union to ward off the risks that foreign investments present to Europe's security and economic openness. Moreover, it would assist smaller EU member states, many of which have no national mechanism for screening foreign investments.[23] To substantiate the proposal, Commission president Juncker used his State of the Union address to outline: (1) a European framework for the screening of investments at member state level, (2) a cooperation mechanism between member states and the Commission, which can be activated when foreign investments in one or several member states may affect the security or public order of another, and (3) a European screening mechanism for investments affecting projects and programmes of Union interests.[24]

While these proposals received strong support from the Union's major economies, not all member states are equally enthusiastic. [25] In June, an ad-hoc coalition of smaller members (Greece, Malta, the Czech Republic, Sweden, Portugal, Finland and the Netherlands) used a European Council meeting to water down a statement calling on the Commission to examine mechanisms for screening third country investments.[26] Finland's foreign minister Kai Mykkänen even warned that the Commission's plans, while trying to please France and Germany, would risk a trade war with China.[27] In turn, German state secretary Matthias Maching viewed the Council meeting as evidence of growing Chinese pressure on EU members who profit from infrastructure investments.[28]

The incident, as noted by André Sapir, illustrates new lines of division in the European Council.[29] These cleavages, which have become increasingly pronounced since the emergence of China as a major investor in Europe following the European debt crisis, may increasingly complicate the EU's ability to develop and implement measures for dealing with China collectively. They also may impact ongoing Sino-European negotiations over a bilateral investment agreement. This agreement, through which Europeans seek to establish a level-playing field in investment relations, has great potential for strengthening the BRI's 'win-win' potential. The EU's success in negotiating this agreement, for which they may use Europe's market size and China's growing interests as an investor as levers, however, hinges on the capacity of member states to act as a united group. With China growing ever more influential, especially in the EU's periphery, this capacity has become increasingly uncertain.

Conclusion

In his State of the Union address, Commission president Jean-Claude Juncker chose strong words to address the challenges arising from China's investment campaign: "Let me say once and for all: we are not naïve free traders. […] If a foreign, state-owned, company wants to purchase a European harbour, part of our energy infrastructure or a defence technology firm, this should only happen in transparency, with scrutiny and debate".[30] While his rhetoric sent a clear message to China, signalling the EU's fading patience with a persistent lack of reciprocity, it also called on member states to stand united and support the Commission's proposal for a European investment screening mechanism. The lukewarm support of some member states for the Commission's initiative should set alarm bells ringing. The Union cannot afford to appear disunited or indecisive considering the economic and political challenges the BRI presents to Europe. The Commission's struggle to gather support for an instrument that every major economy (including the US, China and 12 EU member states) applies to ensure their security and public order, raises questions about the EU's capacity to deal with China in a meaningful and collective way. Restoring unity among member states vis-à-vis China therefore constitutes an increasingly pressing task to which EU institutions should assign the highest priority. After all, only a united EU will be able to push for the investment regulations and standards necessary to turn the BRI into a project that benefits both Chinese and European businesses and citizens.

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