CHINA'S EUROPEAN CENTURY

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INTRODUCTION

While the U.S. is shifting its strategic focus to Asia (the "Asian Pivot"), China is rapidly intensifying its relations with Europe – and appears to be filling the strategic gap left there by Washington. As Chinese investment in (and trade with) Europe grows, so does Beijing's influence on EU politics.

In an online, crowdsourced analytic exercise, Wikistrat's experts recently predicted that the coming years will see a deepening of this China-Europe interdependence.

BACKGROUND

At the end of June 2015, Chinese Premier Li Keqiang urged European policymakers to begin negotiations for a Chinese-European investment treaty. Li requested the EU lower – or even abolish – existing trade barriers (e.g., tariffs), as the higher rate of exchange of goods and products would be a boost for both economies. Reaching such an agreement will be long and time-consuming, but the appeal to start negotiations at this time fits into the bigger picture of China's economic shift towards Europe.

In November, China hosted political leaders of Eastern European states to discuss deepening cooperation at the so-called "16+1 Summit". The aim was to integrate Eastern European economies into the comprehensive New Silk Road project, thereby intensifying regional trade and opening Western European markets for Chinese goods. With massive investments in required infrastructure projects, Beijing will gain in two respects: new orders for China's huge construction industry, and favorable relations with the countries where these infrastructure projects are realized. Poland already considers itself to be Europe's upcoming logistics center.

TRADE ROUTES

Western Europe is both the world's largest single market and the most important for both China and the United States. Indeed, the European market is a key final destination – especially for sophisticated electronics and other consumer products. Notably, the high average income of Europe's consumers results in a purchasing power critical for producers.

Total trade between the EU and China increased from €178 billion in 2004 to €467 billion in 2014. Given the average growth ratio of this period, China-EU trade will grow to approximately €650 billion by 2020. However, this projection is based on old growth rates; China's recent efforts to increase trade by improving trade logistics will probably lead to higher numbers in this respect.[1]

China already ranks as the EU's number-one partner with regard to imports and is the EU's number-two exports destination. Trade between China and Europe is dominated by industrial/manufactured goods, which represent over 90 percent of all bilateral trade.

China is putting significant effort into upgrading and modernizing land and maritime trade routes with Europe. The land-based trade route – the so-called New Silk Road – connects China with Europe via Central Asia, Iran and Turkey. This trade route is already operational; it takes two weeks for a freight train to traverse it. But the route's logistical infrastructure is underdeveloped. The recently established Asian Infrastructure Investment Bank (AIIB) is designed to finance infrastructure projects; a main focus thereof will be upgrading the facilities along the New Silk Road.

The establishment of the AIIB – which took place despite the opposition of Washington – had 57 founding members, including key U.S. allies like the U.K. and Germany. 70 percent of the organization capital, however, originates from within the Asian region – thus guaranteeing China's influential role. China's overall stake is 30 percent and its voting share is 26 percent, thus providing it with the power to veto projects. The *Financial Times* called the establishment of the AIIB "China's most ambitious foray into financial diplomacy."

As a further trade route initiative, China is investing in port facilities to improve maritime trade with Western Europe in a project known as the Maritime Silk Road. This trade

[1] European Commission (2015): "European Union, Trade in goods with China", available at: http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113366.pdf

pathway connects China with Europe via harbors in the South China Sea, the Indian Ocean, the Red Sea and the Mediterranean. Key new ports along this trade route are in Pakistan's Gwadar and Kenya's Nairobi. Additionally, Greek ports (Piraeus and Thessaloniki) will be used as transshipment points, where container-handling facilities are already operational and will be upgraded by Chinese investments.

FINANCE

Trade between Europe and China is still handicapped by exchange rates between the Euro and Renminbi (RMB). Frankfurt, however, has recently been appointed as a clearing point for China-Europe transactions, and the Bank of China, with German Bundesbank support, is establishing a clearing system. The establishment of this clearing point for China-Europe transactions is an important step by which to improve investment procedures, and is critical for trade relations between the world's "workbench" (China) and the world's largest single market (Europe). In London, the overall trading volume in RMB has doubled since 2014. Just recently, the London Metal Exchange (LME) has agreed to accept the RMB. This represents a validation of China being the world's top consumer and producer of most metals. It fits well into this picture that in December, the IMF decided to accept the RMB as a reserve currency (effective by October 2016).

These recent developments will further solidify the RMB as a global currency – and with it, China's growing economic and financial stature: In 2014, the RMB was the seventh-most-used currency in the world. In 2015, it is already the fifth-most-used currency.

EUROPEAN BRIDGEHEADS

As outlined above, China's investments are meant to improve the New Silk Road and Maritime Silk Road with regard to travel speed, operability and safety. Better logistical infrastructure will facilitate trade between China and Europe, as well as trade between China and the markets along these routes. Key points for China's investments in Europe are trade hubs in Greece and Bulgaria. Both countries present great opportunities in terms of low labor costs and investment possibilities. They therefore qualify as bridgeheads in Beijing's economic strategy and will attract further Chinese investments in the future. While China's investment in Europe was negligible in the year 2000, it soared to amounted direct investments of €14 billion in 2014. The focus of China's investment has thus far been the U.K., Germany and France (in this order), as Chinese investments have been concentrated on sophisticated industrial producers. Future Chinese investments will also focus on strategic logistical locations.

CHINA TURNS WEST: OPTIONS FOR THE U.S.

The U.S. pivot to Asia is at its core a geopolitical, security-driven move conceptualized on strategic military assessments. By contrast, China's turn to Europe lacks similar security and military characteristics (save the anti-terror efforts in Central Asia which China is conducting in concert with Russia via the Shanghai Cooperation Organisation). China's focus is instead on trade relations and investment – and has a distinct possibility of finding success.

The U.S. and Europe have been negotiating the Transatlantic Trade and Investment Partnership (TTIP) for several years now; however, several disagreements have yet to be resolved, and the outlined timeframe to reach an agreement had to be postponed again this July. The U.S. should push for this trade agreement and win the consumer and industry market shares in Europe before Beijing's companies have laid the groundwork for China's European Century.

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