Europe’s Response to China’s Activism
Balancing Hope and Fear in the New Age of Global Economic Governance

Maaike Okano-Heijmans
Daniel Lanting

Clingendael Report
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Executive Summary

The summer of 2015 proved to be turbulent for the Chinese government and economy. After rapid gains in the stock market in the previous months, the bubble burst and stocks started to fall on 12 June. Since then, the market has been in near constant decline. The Chinese government stepped in to attempt to stabilize the market, enacting measures ranging from stopping short-selling and initial public offerings, to instructing pension funds to buy more and providing brokers with extra cash from the central bank. Amid these market troubles, the government decided to devalue the renminbi by the largest amount in two decades, triggering similar devaluations across the globe. These actions by the Chinese government relate to a more fundamental debate about the direction of China’s economy and its politics. Is the government rolling back the market-driven reforms of recent years and taking a more central role in running the economy? Or are these just temporary fixes that are characteristic of a country in economic transition? And what are the implications of China’s political economic transition for other leading economies and for Beijing’s recent attempts to exert greater leadership in global economic governance?

Answers to these questions are of paramount importance for Europe as well. China and the European Union (EU) are increasingly economically intertwined, with trade between the two currently standing at well over US$ 1 billion a day, and the EU being China’s largest trading partner, while China is the second-largest for the EU. As a result, many of China’s choices on how it wishes to govern both its domestic political economy and the future international order will impact the EU and should be considered accordingly.

This Clingendael Report provides an overview of the various Chinese actions, goals and strategies in the field of global economic governance and discusses how these impact on the EU’s ability to pursue its own goals in this area. China’s pursuit of a greater role in the international economic order is pragmatic, opportunistic and self-interested – much like other big, developed powers, such as the United States, Japan and the EU. Inevitably, Chinese interests will align with European interests on certain fronts, while diverging on others. So far, however, there is a lack of in-depth studies detailing the commonalities and divergences in interests from a European perspective. Clearly, this obfuscates the development of a more sophisticated response to China’s activism, which is needed in order better to defend European interests.

One of this report’s key conclusions is that a shared European framework on how each of Beijing’s goals impact on European political and economic interests is required to press China to conform to Western standards as it unfolds its own policies. To the extent that interests align, European capitals are right to welcome the increasingly stronger
role and responsibility of China in global economic governance. This also means that European capitals should recognize that certain long-standing practices can be improved, based on insights of rising powers. Where interests diverge, however, the EU and its member states benefit from the binding of forces, by which they have shown themselves to be better able to defend the standards and norms that took decades to develop. This is important, as more than a few policy-makers seem to believe that China's international activism stems from a belief in multilateralism per se. China, however, is not like Europe on this front.

**China’s Multi-pronged Approach**

The establishment of two new China-led financial institutions in early 2015 – the Asian Infrastructure Investment Bank (AIIB) and the New Development Bank – add urgency to the call for strengthened strategic thinking on the topic of global economic governance in Europe. Even if much is still unclear about the operations of the new banks, they are evidence of Beijing’s ambitions in reshaping the system of global economic governance. Such activism is likely to be maintained and further developed. The days in which Europe and the United States largely decided what would happen in this field are over, and these new initiatives are indicative of the direction that global governance as a whole is likely to be heading.

The creation of new institutions is just one arm of Beijing’s multi-pronged approach to reshape global economic governance. From reforms in the Bretton Woods institutions to chairing the G20, China’s presence is felt in every forum and organization. Even the Organization of Economic Cooperation and Development (OECD), of which China is not a member, is confronted by the growing relevance of China on the world stage. By the end of 2015, the International Monetary Fund (IMF) will review its currencies basket of Special Drawing Rights (SDR), in which the possible inclusion of the Chinese renminbi is a point of key contention. This provides yet another example of the relevance of examining the combined effects of China’s actions across this field.

As well as Beijing’s activism in establishing new institutions and reshaping the existing institutional architecture, China is also carving out a greater role for itself through the promotion of international networks of its choice. Two key topics that often adorn the front pages of newspapers these days are China’s ‘One Belt, One Road’ initiative and the bilateral and regional trade deals that are being negotiated. Less well known but of particular relevance to Europe is the China–Central and Eastern Europe framework (CCEE, or ‘16+1’).

In October 2015, a total of twelve countries across four continents reached agreement on the biggest trade and investment deal in two decades, the US-led Trans Pacific Partnership (TPP). China is not part of this agreement for the time being, and as such
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is feeling the pressure as countries in its region are signing up to one of the most far-reaching trade deals ever negotiated. In response, Beijing is promoting two competitive networks of regional trade multilateralism.

On the other side of the globe, the world’s two largest economies, the EU trading bloc and the United States, are negotiating their own trade and investment deal, the Transatlantic Trade and Investment Partnership (TTIP), which will further raise the standards and practices for trade agreements. These two agreements – the TPP and TTIP – are placing enormous pressure on China and its hopes of bending the system of global economic governance in its favour. This context shapes Beijing’s interest in forging an investment deal and, eventually, a free-trade agreement with the EU.

The other topic frequently discussed is the Chinese ‘One Belt, One Road’ initiative, also referred to as the Silk Road Economic Belt and 21st-century Maritime Silk Road. Official Chinese state visits in recent times have almost all involved discussions or agreements about this current priority in Chinese foreign policy. The wish to connect the European market with China through Central Asia and Africa would be a major step for China in its global ambitions. The ‘16+1’ initiative aims to contribute to this goal through its engagement with a mix of EU and non-EU countries in the Central and Eastern European region. This Chinese initiative has aroused suspicion in EU institutions, which share the competence to govern on transport with the EU member states, about both Beijing’s intentions and the EU member states’ loyalties.

As China is gaining a stronger voice in global economic governance, both within the more established Bretton Woods institutions and by its leading role in new institutions and networks, a better understanding of Beijing’s underlying assumptions and ultimate goals is of crucial importance to European capitals. In this sense, discussions of whether China is a status-quo power or a challenger seem to miss the point, as they forego the fact that China can – and does – also modify the existing system from within.

**Beijing’s Three Principal Aims and their Impact on Europe**

The principal objectives of China’s activism in global economic governance can be summarized as follows: (1) strengthening China’s influence and status in economic governance; (2) furthering domestic objectives through foreign policy; and (3) promoting acceptance of new standards and changing the rules of the game of international politics and economics. Analysing these aims that Beijing is trying to achieve for itself is paramount for answering the question of how China’s activism impacts on European interests.

The key question that European capitals should ask themselves is how practices, standards and norms would be different if Beijing had things its way, and how this would
affect European interests and the ability of European capitals to defend their interests. Sacrifices to existing standards may be the result of responding to actual demands from Beijing and from pre-emptive compromise by established powers. Analysis in this report shows that both processes are under way.

These processes are slow and often muted, and are thus easily overseen; they are spurred by the continuous evolution of policy over time, as well as by growing competition and financial hardship that comes with the changing balance of global economic power. Examples are found on various fronts: in the World Trade Organization (WTO), where China’s market-economy status is up for debate; in the IMF, where inclusion of the Chinese renminbi into the SDR is being discussed; in the OECD, whose members are now discussing a redefinition of official development assistance; and in the AIIB, which European countries joined before knowing what the institution would be like. To some extent, these changes are only natural. Problematic, however, is the fact that in Europe – at the EU and member-state level – strategic thinking on China lags behind rapidly evolving practice, resulting in an ever-growing discrepancy between medium- and long-term interests and short-term action.

Maintaining Oversight... and Diversity in Representation

This Clingendael Report finds that European countries are generally better able to coax Beijing to agree with measures that are generally out of its comfort zone when using their combined strength. There are various ways to achieve this: through joint representation (such as in trade negotiations); proper coordination (as in the IMF); or, at the very least, through a common framework (as with Europe’s more timely response to the Silk Road initiative). A significant variety of formats of representation may be considered in the various forums of global economic governance (such as the EU-28, Eurozone countries, other groupings of EU member states, or member states individually) and best practices should be sought on a case-by-case basis. That being said, EU member states are well-advised to improve their strategic capacity and oversight at the EU level. One necessary step in this regard is re-establishment of the China taskforce that existed prior to the bureaucratic struggle that came with the 2009 Lisbon Treaty.

European capitals play an important role in Beijing’s global economic governance strategy. The faulty, lagging response by the EU to China’s AIIB initiative served as a wake-up call to many in Europe. While there is no need to develop one answer or one voice for everything, a shared European framework would provide a more coordinated and aligned approach towards cooperation with China, at least on larger strategic issues. Such a coordinated approach requires a strategic, comprehensive and long-term assessment of the EU and its member states’ priorities and interests in the relationship with China. This Clingendael Report should be read as a contribution to discussions to achieve this objective.
### Abbreviations

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<th>Abbreviation</th>
<th>Full Form</th>
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<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
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<td>ADBC</td>
<td>Agricultural Development Bank of China</td>
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<td>AEC</td>
<td>ASEAN Economic Community</td>
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<td>AIIB</td>
<td>Asian Infrastructure Investment Bank</td>
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<td>APEC</td>
<td>Asia–Pacific Economic Cooperation</td>
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<tr>
<td>ASEAN</td>
<td>Association of South-East Asian Nations</td>
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<td>ASEM</td>
<td>Asia–Europe Meeting</td>
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<td>BIS</td>
<td>Bank of International Settlements</td>
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<td>BRICS</td>
<td>Brazil, Russia, India, China and South Africa</td>
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<tr>
<td>CCEE</td>
<td>China–Central and Eastern Europe framework ('16+1')</td>
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<td>CCP</td>
<td>Chinese Communist Party</td>
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<td>CDB</td>
<td>China Development Bank</td>
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<tr>
<td>CEE</td>
<td>Central and Eastern Europe</td>
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<tr>
<td>CFSP</td>
<td>Common Foreign and Security Policy (EU)</td>
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<tr>
<td>CJK</td>
<td>China–Japan–Korea ('Trilateral')</td>
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<tr>
<td>CMIM</td>
<td>Chiang-Mai Initiative Multilateralization</td>
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<tr>
<td>COASI</td>
<td>Asia–Oceania Working Party (EU)</td>
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<td>COREPER</td>
<td>Committee of Permanent Representatives (EU)</td>
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<tr>
<td>CRA</td>
<td>Contingent Reserve Arrangement</td>
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<tr>
<td>CSDP</td>
<td>Common Security and Defence Policy (EU)</td>
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<tr>
<td>DAC</td>
<td>Development Assistance Committee (OECD)</td>
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<tr>
<td>DG</td>
<td>Directorate-General</td>
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<tr>
<td>DG DEVCO</td>
<td>Directorate-General for International Cooperation and Development (EU)</td>
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<tr>
<td>DG ECFIN</td>
<td>Directorate-General for Economic and Financial Affairs (EU)</td>
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<td>DG MOVE</td>
<td>Directorate-General for Mobility and Transport (EU)</td>
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<td>DG TRADE</td>
<td>Directorate-General for Trade (EU)</td>
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<tr>
<td>DSB</td>
<td>Dispute Settlement Body (WTO)</td>
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<tr>
<td>EBRD</td>
<td>European Bank for Reconstruction and Development</td>
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<tr>
<td>EC</td>
<td>European Commission</td>
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<tr>
<td>ECB</td>
<td>European Central Bank</td>
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<tr>
<td>ECOFIN</td>
<td>Economic and Financial Affairs Council (EU)</td>
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<tr>
<td>EEAS</td>
<td>European External Action Service</td>
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<td>EEU</td>
<td>Eurasian Economic Union</td>
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<td>EFC</td>
<td>Economic and Financial Committee (EU)</td>
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<td>EFSI</td>
<td>European Fund for Strategic Investments</td>
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<td>EIB</td>
<td>European Investment Bank</td>
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<tr>
<td>EIBC</td>
<td>Export–Import Bank of China</td>
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<tr>
<td>EIF</td>
<td>European Investment Fund</td>
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<tr>
<td>Acronym</td>
<td>Full Form</td>
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<tr>
<td>EMU</td>
<td>European Monetary Union</td>
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<td>EU</td>
<td>European Union</td>
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<tr>
<td>FDI</td>
<td>Foreign direct investment</td>
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<tr>
<td>FSB</td>
<td>Financial Stability Board</td>
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<tr>
<td>FTA</td>
<td>Free-trade agreement</td>
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<td>FTAAP</td>
<td>Free-trade Area of the Asia–Pacific</td>
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<td>GDP</td>
<td>Gross domestic product</td>
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<tr>
<td>G7</td>
<td>Group of Seven (major advanced economies)</td>
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<td>G8</td>
<td>Group of Eight (industrialized nations)</td>
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<td>G20</td>
<td>Group of 20 (major economies)</td>
</tr>
<tr>
<td>IA</td>
<td>Investment Agreement</td>
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<tr>
<td>ICT</td>
<td>Information and communications technology</td>
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<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
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<tr>
<td>IMFC</td>
<td>International Monetary and Financial Committee</td>
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<tr>
<td>IPR</td>
<td>Intellectual property rights</td>
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<tr>
<td>ISDS</td>
<td>Investor-state dispute settlements</td>
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<tr>
<td>MDB</td>
<td>Multilateral development bank</td>
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<tr>
<td>NDB</td>
<td>New Development Bank</td>
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<tr>
<td>NGO</td>
<td>Non-governmental organization</td>
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<tr>
<td>NPC</td>
<td>National People's Congress (China)</td>
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<tr>
<td>OBOR</td>
<td>‘One Belt, One Road’</td>
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<tr>
<td>ODA</td>
<td>Official development assistance</td>
</tr>
<tr>
<td>OECD</td>
<td>Organization for Economic Cooperation and Development</td>
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<tr>
<td>PBoC</td>
<td>People's Bank of China</td>
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<tr>
<td>PPP</td>
<td>Purchasing Power Parity</td>
</tr>
<tr>
<td>PRC</td>
<td>People's Republic of China (China)</td>
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<tr>
<td>RCEP</td>
<td>Regional Comprehensive Economic Partnership</td>
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<td>RMB</td>
<td>Renminbi</td>
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<tr>
<td>SCO</td>
<td>Shanghai Cooperation Organization</td>
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<tr>
<td>SDR</td>
<td>Special drawing rights</td>
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<tr>
<td>SG</td>
<td>Secretariat-General (EU)</td>
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<td>SME</td>
<td>Small and medium-sized enterprise</td>
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<tr>
<td>SOE</td>
<td>State-owned enterprise</td>
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<tr>
<td>TFEU</td>
<td>Treaty on the Functioning of the European Union</td>
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<tr>
<td>TPP</td>
<td>Trans-Pacific Partnership</td>
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<tr>
<td>TTIP</td>
<td>Transatlantic Trade and Investment Partnership</td>
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<tr>
<td>US</td>
<td>United States</td>
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<td>WTO</td>
<td>World Trade Organization</td>
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Introduction

Over the past decade, new power alliances, multilateral institutions and networks have emerged in the international system. Taken together, these processes are altering the organization and dominant practices that have characterized the world of international politics and economics since the mid-twentieth century. As the biggest country in the BRICS group (that is, Brazil, Russia, India, China and South Africa), with a political–economic system and values that differ significantly from those of developed countries, China is playing a key role in this change. Since taking power in March 2013, Chinese President and Secretary-General of the Communist Party Xi Jinping has been steadily unfolding a more proactive approach to reshaping global economic governance. This activism contrasts with the low-profile approach of Xi’s predecessors, and is likely to be maintained and even further developed. As the old, overrepresented continent in today’s system and with relatively weak ties to China other than in the economic field, much is at stake for Europe.

Given this context, this Clingendael Report raises several questions about Europe, China and global economic governance. How does China’s activism impact on the interests and the influence of the European Union (EU) and its member states in the international system of global economic governance? Do the various Chinese initiatives strengthen or rather undermine the coherence of the EU and its ability to speak with one voice? More specifically, is Europe becoming more vulnerable in terms of economic security? Finally, have the EU and its member states been able to develop a coherent response to China’s endeavours? These questions obviously relate to the role that China and Europe see for themselves in tomorrow’s world, and to the question of which alliances, institutions and values are likely to be most influential.

To answer these questions, the report seeks an overall, integrative perspective to this complex issue by reviewing Beijing’s activism in reshaping global economic governance and the consequences for Europe. As China seeks a greater role in economic governance processes, it pursues a combination of approaches involving both the existing architecture and new institutions and networks. Today, specific Chinese undertakings in this field are the subject of much debate. What is often lacking, however, is a weighted analysis of the effects of Beijing’s undertakings on EU cohesiveness and, by extension, on the effectiveness of Brussels and European capitals to advance their own policies successfully. Such a comprehensive approach lends itself to understanding and demonstrating the combined effect of China’s activism on Europe and to developing appropriate responses.
EU–China Relations Intensifying, Diversifying

Visiting Brussels at the height of the Greek debt crisis during the EU–China Summit in June 2015, Chinese Premier Li Keqiang presented China as ‘a true friend of the European Union’, adding that it wants ‘a prosperous EU, a united Europe and a strong Europe’. Europe can certainly use a share of the US$ 4 trillion in reserves that Beijing holds. Moreover, China wants to invest. With the Asian Infrastructure Investment Bank (AIIB), the Silk Road initiative, negotiations on economic agreements, and participation in the Juncker Investment Plan, Beijing is promoting a series of initiatives that ultimately aims to strengthen its domestic economy as well as its influence in the world. Europe has much to gain from this as well. Yet a key message put forward in this report is that the EU and its member states should not inadvertently help to lay the grounds for a world in which Chinese preferences dominate.

The authors of this report point out that China’s challenges to the existing international system of politics and economics are threefold. First, Beijing aims to strengthen its influence in existing institutions, calling for institutional reform and using its membership to expand its role in global economic governance. This is mainly seen in the World Bank, the International Monetary Fund (IMF), the Asian Development Bank (ADB), the World Trade Organization (WTO), the G20 and the Organization for Economic Cooperation and Development (OECD). Second, China is establishing alternatives in an attempt to counter the ‘Western-dominated world’ that these institutions are said to represent. Examples of such new institutions are the AIIB, the New Development Bank (NDB, or BRICS Bank) and the Contingent Reserve Arrangement (CRA). Third, China is launching new cooperative organs and initiatives that do not build on or respond to existing forums, but rather create new networks. Examples of these are the Silk Road Economic Belt and Maritime Silk Road, and the China–Central and Eastern Europe platform (CCEE, or ‘16+1’). In the international trading system, China’s attempts to further the Asia–Pacific Economic Cooperation (APEC)-led Free Trade Area of the Asia–Pacific (FTAAP) as well as the intra-Asian Regional Comprehensive Economic Partnership (RCEP) are paramount, and run parallel to talks on an EU–China bilateral investment treaty.

While the Chinese government seeks to create flexible, cooperative coalitions to further many of these undertakings, it takes the lead or acts on its own in more than a few of them. This distinguishes China from other emerging economies, such as India or Brazil, which may challenge the international system in cooperation with others but are hardly capable of – or indeed interested in – adding major (value) propositions of their own. Notably, Beijing directly engages with more traditional elements of the international system in the first and third of the above-mentioned sets of initiatives. By contrast, it has taken the initiative towards and/or is the dominant actor in each of the other undertakings, which thereby illustrate other elements of China’s strategy, ambitions and interests. Importantly, these differences also make for variations in the impact of China’s
activism on the EU and its member states (either individually or in groups), and on their ability to exert influence.

As China under Xi Jinping is determined to become an agenda-setter in Asia and beyond, the need for the EU and its member states to clarify their own priorities and positions in the wider Eurasian space is now more urgent than ever. Building on the results of such an understanding, Europe needs to develop a coherent response or risks losing the opportunity to speak with one voice where possible, and to develop a pragmatic response at the national level where needed. Clearly, European countries stand to gain from Chinese activism in the field of global economic governance. Yet it is only by having a shared European framework for how each of Beijing’s goals impacts on European political and economic interests that EU capitals will really be able to press China to conform to their standards as Beijing unfolds its own policies.

**Methodology and Structure**

This qualitative international relations analysis employs a varied set of tools for data-gathering and analysis. Data-gathering included desk studies of relevant primary sources (including official statements, diplomatic interactions and media coverage), as well as of policy-oriented and scholarly analysis. In addition, the authors conducted semi-structured interviews with more than 30 relevant policy-makers and scholars from the Netherlands and EU institutions, so as to cross-check and illustrate findings. Officials and experts from other countries in Europe and Asia were also consulted.

The analysis is structured around one leading question: how do China’s attempts to (re)shape institutions and networks of global economic governance impact on Europe’s ability to further its own interests? Answers to this question are sought through an analysis of three core strategic goals that China is trying to achieve for itself, followed by an assessment of how these goals impact upon Europe. China’s goals are: (1) strengthening its influence and legitimacy in economic governance; (2) furthering domestic objectives through foreign policy; (3) promoting acceptance of new standards and changing the rules of the game of international politics and economics. The three objectives are obviously multifaceted and interrelated, as a strengthened Chinese position in global economic governance plays a vital role also in achieving the other two goals. A better and comprehensive understanding of the strategies and goals of the Chinese government is crucial as Europe defines appropriate responses to secure its own position.

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1 Ekman, 2015, p. 4.
2 These strategic objectives of Chinese leaders were identified from an analysis of leadership statements, diplomatic interactions, media coverage and scholarly analysis.
Clearly, domestic economic goals feature prominently in China’s activism overseas. That is to say, foreign policies in the field of global economic governance aim to support the domestic economic development and reforms that are desired by Chinese leaders. This report considers these domestic economic goals to the extent that they impact significantly on European interests. As a result, a relatively large amount of attention is paid to the strategic goals pursued by the Chinese government. While the overview of Chinese aims presented here is thus by no means exhausting, the issues considered do stand out as the most important.

Towards a System with Chinese Characteristics

Two narratives tend to dominate discussions about China’s ambivalent approach to economic multilateralism. One side argues that the evidence of China’s interaction with the existing system of global economic governance points towards Chinese convergence on the status quo of the existing infrastructure. Proponents of this view suggest that the impact of the large emerging economies on global governance is unlikely to be revolutionary. It is argued that China, in most of its interactions, follows the same path as other countries, seeking to maximize its own gains while minimizing the loss of autonomy. The competing vision, meanwhile, emphasizes that China is in effect challenging the status quo, because its political and economic systems – characterized as a state-led market economy – are inherently incompatible with some fundamental liberal characteristics of the existing economic organizations.

The debate hence centres on the question of to what extent China would be willing to accommodate or to seek to change the existing system. Instead, however, this report argues that such debates are important only if they lead to questions of what a new Chinese-influenced system will look like; and how this will affect the EU’s ability to pursue its own vision of global economic governance. To this effect, a better understanding is required of China’s main strategic objectives, its national interests, traditions and culture, and of the extent to which these interests are likely to change in the medium-term future, namely the coming ten to 25 years.

There can be little doubt in certain areas of global economic governance that China’s status as a non-democratic society and state-led market economy conflicts with the existing system. This logically follows from three important characteristics of the Chinese

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3 Kahler, 2013, p. 712.
4 Nölke et al., 2014.
5 Considering China’s tendency to use five-year plans, fundamental policy change should not be expected in the short-term future, barring a crisis. The long-term future – that is, a period further away than 25 years – is more difficult to foresee and therefore beyond the scope of this study.
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political-economic system, namely: (1) major Chinese companies are dominated by national capital and not transnational financial investors, and these companies raise money through loans from national banks at favourable rates; (2) the patent rights system in China is significantly weaker than in other parts of the world, and foreign companies’ patents and innovation are not carefully protected; and (3) China selectively integrates into the global economy and continues to protect domestic markets from foreign investment.

Clearly, these characteristics challenge some of the basic notions of free and fair trade promoted by the WTO and other agreements on services and investment. Some sectors in China remain closed to foreign investment, while foreign companies in other sectors are forced to set up joint ventures, or ceilings exist on the amount of foreign share ownership. Additionally, while the IMF believes in the importance of liberal capital accounts, which allow for free foreign trading of government bonds, the difficulty of buying these bonds shows that this is not the case in China.

The continued influence of the Chinese state on the economy has been paralleled in recent years with stricter policies on the socio-political front, including the growing repression of civil liberties and reversal of political reforms. While this in itself should make European governments think about human rights standards, the negative effects from restrictive policies, including internet freedom, also extend to the field of trade. For example, a rather vaguely phrased national security law introduced in July 2015 could force foreign companies in China – particularly technology firms – to expose intellectual property further. Furthermore, the arrest in August 2015 by Chinese authorities of journalists and other individuals for (online) rumor-mongering about China’s stock market turmoil can lead to greater market volatility.

While the compatibility of the WTO and national security law is still up for debate, such characteristics – which to some extent distinguish China from developed economies in Europe – do not necessarily make China incompatible with the existing institutions of global economic governance. After all, over the past decade, Beijing has been invited to join and engage with existing institutions, and from the point when China started to open up in 1989, it has accepted the international system and not challenged it. China

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6 This follows Nölke et al., 2014
7 Shambaugh, 2015.
8 Godement and Kratz, 2015.
10 Van Pinxteren, 2015.
developed with the help of World Bank loans and it has been an increasingly active member of the WTO. China has overall benefitted – and still benefits – from the existing architecture and therefore has little reason to attempt to overthrow the existing system.

**Chinese and European Interests Aligned?**

Even if China does not wish to overthrow the current system, it does have ample reason to want to improve its own position in global economic governance. Lagging reform in the IMF and, to a lesser extent, the World Bank has added fuel for this. China is thus launching initiatives of its own, in addition to seeking adjustments in existing institutions and to established practices and standards.

Importantly, such change does not only come through voting reform or other systemic adjustments. A more indirect challenge from China’s different political economic system comes from its indirect power to influence, by which its actions spur modifications in practices of developed economies, even without China asking for them. Such informal ways by which China succeeds in reshaping the system of global economic governance are apparent, for instance, in the development assistance arena. Here, the emergence of new actors, including China – especially in Africa – and economic and financial hardship at home have spurred developed countries to emphasize increasingly the economic rather than social approach themselves. In addition, the definition of official development aid (ODA) is being renegotiated towards acceptance of greater shares of loans. A similar process is ongoing in the IMF, where Beijing is altering the standards of currency convertibility to conform increasingly with its own vision of managed convertibility.¹²

Change in long-held practices spurred by Chinese influence may constitute welcome and at times long overdue adjustments. It is also likely, however, that modifications will result in a lowering of standards that took decades to develop. This would spur the creation of a less demanding but also a less ambitious system of global economic government, in which increased competition impels governments and other actors – including the private sector – to lower the quality of their offer in order to stay competitive. The implications of China’s activism should thus be considered on a case-by-case basis, and with an eye on their long-term consequences and effect on the existing system.

What distinguishes China from other countries – including India and Russia today, and Japan several decades ago – is that it combines huge capabilities with a fundamentally different system that is showing little inclination to conform to neo-liberal standards,

¹² For more on this, see chapter two of this Clingendael Report.
at least in the short to medium term. The fact that China is the world's second-biggest economy, with a population bigger than the EU, United States (US) and Japan combined, makes it more capable to change the system in ways that others could not and cannot. Its conflicting interests as a non-democratic society and state-led market economy suggest that Europe, for the time being, should not overly accommodate the creation of a world wherein Chinese standards are more influential.

About this Report

This report proceeds as follows. Chapter one explores the responsibilities and representation of the EU and its member states in the field of global economic governance. Chapter two presents an assessment of how China seeks to further its interests within the existing Bretton Woods institutions, as well as other organizations of global economic governance where Western economies are most influential. The discussion covers the World Bank, the IMF and the WTO, as well as the G20, the OECD and the ADB. Chapter three proceeds with an analysis of how Beijing advances its interests through the creation of new institutions of global economic governance, in particular the AIIB, the NDB and the CRA. Chapter four assesses Chinese interests in furthering non-institutionalized but multilateral networks in the Eurasian sphere. Most important in this regard are the ‘One Belt One Road’, or Silk Road initiative, the ‘16+1’ framework and regional trade talks in various settings. Each of the three chapters examining Chinese activism in global economic governance ends with a concluding paragraph on the implications for Europe. Complementing this, Chapter five addresses the question of whether and how a common response of the EU and its member states to Chinese activism in the field of global economic governance is feasible. It does so by returning to the question of European representation and coordination, and by assessing the consequences of recent developments for EU–Asia cooperation and transatlantic cooperation. Concluding that a shared framework to engage and confront China is both necessary and feasible, the report ends with an overview of the options and likely consequences in this regard for European capitals.

This study forms part of a project that was funded by the Ministry of Foreign Affairs of the Netherlands. Clingendael’s project team and its sponsor jointly defined the aims of this report, but Clingendael carried out the study independently. The views expressed in this report do not necessarily express those of the sponsor.

13 Other written output from this project includes two opinion pieces and one article in a popular magazine: Okano-Heijmans, 2015; Okano-Heijmans and Lanting, 2015; and Okano-Heijmans and Van Pinxteren, 2015. In addition, a closed expert seminar on the subject took place at the Clingendael Institute on 21 September 2015, with participants from the public and private sectors, as well as academia from the Netherlands, in particular.
Europe in the World: Responsibility and Representation

Europe plays an important role in Beijing's series of initiatives that ultimately aim to strengthen its domestic economy as well as its influence in global economic governance. China’s flagship Silk Road initiative ends in Europe. Moreover, European capitals respond more positively to Chinese moves to reshape governance than other established powers, especially the United States and Japan, as is evident from their greater willingness to reform traditional institutions such as the IMF and to join the newly established China-led AIIB.

This more constructive stance gives European capitals significant influence, in theory at least. The EU’s negotiations with China on a comprehensive investment agreement serve as a good illustration, as this has allowed Europe to pull China closer to its position in areas such as market access, transparency, liberalization of investments and a level playing field for companies. Separately, the European proposal for a Connectivity Platform at the 2015 EU–China Summit showed that the EU is more than a partaker of China-led initiatives. It can also moderate and control the quality of China’s vast ambition to reshape its global economic governance reach.

However, EU member states also compete when it comes to obtaining economic favours from China. From a European perspective, this is undesirable for several reasons. First, individual European countries are highly unlikely to influence China to agree with measures that may be out of Beijing’s comfort zone, in a way that coordinated European action can. Encouraging EU member states to ‘go it alone’ is the most direct way by which China is able to broaden support for its own standards, for example on governance, labour, the environment and civil rights. To divide and rule may not always be a purpose of Chinese policies. Beijing’s dual engagement with European countries at both the bilateral and EU levels, however, does divide EU member states more so than Europe’s more established relations with other powers – such as the United States and Japan. Clearly, as is the case with other powers that more actively employ this strategy, such as Russia, growing divides between EU member states are generally no unwelcome consequence for Beijing.

Second, greater competition between European capitals is more likely to have negative effects on the trade-off between quality and cost, by impelling suppliers to lower the quality of their offer in order to stay competitive. This is an indirect way by which
China makes European capitals change their own perspective, resulting in what has been called a ‘low-cost version of the international order – less ambitious but also less demanding than the outgoing order’\(^\text{14}\) This is exemplified by the rush of 14 European member states into joining the AIIB, without a clear indication of what the rules of the game in that organization would be. As succinctly noted by the *Financial Times*’ David Pilling, ‘from Beijing’s point of view, having Western governments help burnish China’s image in Asia [through the AIIB] must sound pretty close to a definition of soft power’\(^\text{15}\).

**Diverging Governance Models**

The complex division of roles and responsibilities of the EU and its member states in global economic governance adds to Europe’s challenge of responding to Chinese activism in the field. The three models governing the EU – namely EU competence, shared competence and member state competence – apply to different subfields, including but not limited to trade, transport, development, finance and foreign policy. In addition, European representation at times involves more than one EU actor or institution – including various directorates-general and commissioners, as well as the presidents of the European Commission and European Council. This section seeks an overview of this dispersed picture as a prerequisite for identifying good, better and worse European practices.

Of the diverging areas that global economic governance encompasses, it is only in the fields of trade and investment that the EU has been given a clear mandate to act on behalf of all of its member states. The EU – and not individual member states – thus negotiates in the WTO and in regional and bilateral trade and investment negotiations. On behalf of the European Commission, the Directorate-General for Trade (DG TRADE) represents the EU, while the EU member states are consulted. Decisions are made based on a mandate from the Council that is reached through qualified majority voting. Since the 2009 Lisbon Treaty, approval by the European Parliament is required for international agreements in these fields.

In theory, exclusive EU competence also applies to monetary policy for the 19 EU member states that share the euro currency. Nevertheless, Eurozone countries are not jointly represented as a group in any organization of global economic governance. In recent years, discussion has started on whether such joint representation is desirable in the future, for example in the IMF. Proposed joint representation of Eurozone

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\(^{14}\) Godement, 2015.  
\(^{15}\) Pilling, 2015.
countries in the AIIB through a shared seat on the board of this new bank may be seen as a test case.

The EU has shared competence in certain other domains of global economic governance – such as transport, energy, the environment and development. In these limited areas of external policy, the EU is an actor parallel to member states; both the EU and its member states have the power to make laws, but member states lose their power to take decisions when the EU has regulated a certain area. Decisions on these matters are made by a mandate or council conclusions, and EU representation varies. This involves – on different occasions – the rotating presidency, the High Representative for Foreign Affairs and Security Policy, or the European Commission. Table 1 (see below) illustrates in more detail the involvement of specific actors at the EU level.

With regard to international politics and economics, this governance model of shared competence is particularly relevant in the field of development and in more practical undertakings. Consider, for example, the fact that the EU is a formal member of the OECD’s Development Assistance Committee (DAC). It has its own development bank, which distributes roughly one-fifth of development assistance provided by European countries – the European Bank of Reconstruction and Development (EBRD) – as well as a directorate-general in charge of international cooperation and development (DG DEVCO). The mechanism of shared competence between the EU and its member states is also relevant to undertakings under the flag of China’s Silk Road initiative, where the directorate-general for mobility and transport (DG MOVE) is in the lead.17

Responsibility for all other domains of foreign policy that are relevant to global economic governance lies with individual EU member states. This includes the fields of trade and investment promotion and financial issues, and political relations with third countries more generally.18 Even on these matters, however, European member states have all endorsed the political commitment to consult with one another on important matters. This appears to be the reason why the AIIB was on the agenda also in Brussels, including in the Economic and Financial Committee (EFC), the Economic and Financial

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17 In the field of trade, the inclusion of certain sectors – such as visa issues and cultural matters – also requires a special mandate. Interview with an official from DG TRADE, June 2014.
18 Matters of war and peace fall under the framework of the Common Foreign and Security Policy (CFSP) or the Common Security and Defence Policy (CSDP). This third mechanism governing EU external relations, which complements the EU’s exclusive competence and the EU’s and EU member states’ shared competence, is not of much relevance, however, in the field of global economic governance.
Affairs Council (ECOFIN) and the Committee of Permanent Representatives in the European Union (COREPER).

**Who Represents Europe?**

The only institution of global economic governance in which the European Commission is the formal ‘spokesperson’ of the EU in its entirety is the WTO in Geneva. This naturally follows from the EU’s exclusive competence in this field.

The fact that the EU does not have full competence in other areas, however, does not preclude Commission participation in other institutions, along with some or all EU member states being members. Table 1 illustrates this schematically. In the IMF, for example, the European Commission – represented by the Commissioner for Economic and Financial Affairs, Taxation and Customs (DG ECFIN) – and the European Central Bank (ECB) are observers in the International Monetary and Financial Committee (IMFC), while the ECB has observer status also in the IMF Executive Board. Here, they participate in IMF meetings along with representatives of all 28 EU member states.

In the G20, the EU is a full member, along with the four individual EU member countries (France, Germany, Italy and the United Kingdom). Representation is dispersed: the presidents of the European Commission and of the European Council represent the EU at the heads of state and government level, while the European Commission, the ECB and the Council Presidency in the G20 represent it at the finance ministers’ meetings. The same goes for EU representation in the G7 (Group of Seven major advanced economies), with the only difference being that the Eurozone president rather than the Council presidency is one of three representatives at the ministerial level. In relation to this, the EU is also a full member of the Financial Stability Board (FSB), which was announced at the 2009 G20 Leaders Summit, with a mandate to promote financial stability.

The EU is not a member of any of the development banks, except for the EBRD (which in its basic documents explicitly states that this is an exception). With certain other banks, the EU has formal mechanisms of cooperation. In the World Bank, for example, the Commission has observer status in the Bank’s Development Committee – that is, the Ministerial level, where it is represented by the DG ECFIN. In the ADB, European institutions have no formal status – nor any formal cooperation mechanism. European institutions are keen to discuss and cooperate with the AIIB, however, as is evidenced

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19 European Bank for Reconstruction and Development (EBRD), 2013, p. 49. EBRD membership comprises 64 governments, the EU and the EIB.
by the opening of a European Investment Bank (EIB) office in Beijing in June 2015 – to partly cooperate with the AIIB, in addition to cooperating with China to raise funds for the Juncker Investment Plan.20

Table 1  European Representation in International Institutions and Networks

<table>
<thead>
<tr>
<th></th>
<th>World Bank</th>
<th>IMF</th>
<th>WTO</th>
<th>G7 / G20 (♣)</th>
<th>OECD</th>
<th>ADB</th>
<th>AIIB</th>
<th>Silk Road (Land)</th>
<th>Silk Road (Sea)</th>
<th>‘16+1’</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ECB</strong></td>
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<tr>
<td>European Commission</td>
<td>* (♣)</td>
<td>* (♣)</td>
<td>(♦)</td>
<td>Commission President</td>
<td>(♣)(♥)</td>
<td></td>
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<tr>
<td>European Council</td>
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<td>President of the European Council</td>
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<tr>
<td><strong>Euro group (19 total)</strong></td>
<td>18</td>
<td>19</td>
<td>19</td>
<td>3</td>
<td>12</td>
<td>11</td>
<td>11</td>
<td>5</td>
<td></td>
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<tr>
<td><strong>EU member states (incl. Eurozone)</strong></td>
<td>25</td>
<td>28</td>
<td>28</td>
<td>4</td>
<td>15</td>
<td>14</td>
<td>14</td>
<td>1</td>
<td>11</td>
<td></td>
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<tr>
<td><strong>European other</strong></td>
<td>9</td>
<td>9</td>
<td>4</td>
<td>3</td>
<td>5</td>
<td>5</td>
<td>5</td>
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</table>

(♣) At G7 Finance Ministers’ meetings, the EU is represented by the Commission, the ECB and the Eurogroup President. At G20 Finance Ministers’ meetings, the EU is represented by the Commission, the Council Presidency and the ECB.

(♦) Commissioner for Economic and Financial Affairs, Taxation and Customs (DG ECFIN).

(♥) Commissioner for Trade (DG TRADE).

(♠) (Limited) Observer status.

** Officials from the Commission are present to report back on the details of meetings.

*** More European countries – including Hungary and Belgium – intend to join the AIIB at a later stage.

Source: authors’ compilation.

The founding Convention of the OECD gives the European Commission the right to take part in the work of the Organization, enjoying all the prerogatives of membership except the right to vote. In addition, the EU does not make a statutory contribution to the OECD budget. The EU is a full member of a number of OECD committees, most notably the DAC. As in the World Bank, the DG ECFIN represents the Commission for economic

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20 The European Fund for Strategic Investments (EFSI), which went operational on 1 September 2015, is one of the main projects of Jean-Claude Juncker’s European Commission, aiming to gather funds to kick-start the lagging European growth. The Chinese government has expressed interest in investing up to US$ 10 billion in this fund, which is more commonly referred to as the Juncker Investment Plan.
and monetary topics, while the Commissioner in charge of development attends OECD meetings in his area.\(^{21}\)

EU member states are not willing for the time being to give the EU a mandate to apply, despite different EU institutions seeing merit in joining the AIIB as a member.\(^{22}\) This is perhaps the latest example of the ambivalence with which EU member states regard EU participation in global economic governance. Such a reluctant attitude to formalizing EU responsibility is understandable against the background of Brussels’ tendency to pull increasingly more power to European institutions. To the extent that it obstructs a coordinated European message, however, it is likely to be at the expense of the long-term political, economic and strategic interests of EU member states.

If the challenge of developing a common framework is one reason for EU member states to review their coordinating mechanisms and representation at the various multilateral organizations, calls by third countries to do so should be another motivation. For while the broad European representation in the IMF and the World Bank has certain benefits – for example, in terms of voting power and speaking time at meetings – it also induces irritation on the part of others when Europeans constantly repeat the same points during meetings and negotiations.

This is why the merits and pitfalls of different forms of representation in global economic governance deserve closer scrutiny. The various existing and other possible settings by which European countries are represented in institutions of global economic governance include EU-wide representation; constituencies with EU and non-EU members, sometimes including less like-minded countries; or a Eurozone group. Closer analysis of the EU’s ability to defend its interests in these settings furthers our understanding of the pros and cons of speaking with a single voice (like in the WTO), as compared to having a common message (as is done rather successfully in the IMF) or a single, shared framework (as was aimed for, but failed, with regard to the AIIB).

Speaking with one voice as the EU is a power multiplier in certain areas of foreign policy – a phenomenon that has been referred to as ‘the politics of scale’.\(^{23}\) Constant negotiations about who represents the EU and what the EU member states will say can, however, also draw attention away from the problems outside the EU that they are meant to be solving. There are thus reasons why speaking with a *single voice* is not always the

\(^{21}\) DG ECFIN participates actively in certain OECD high-level meetings, while its country desks participate in Economic and Development Review meetings on individual countries. See [http://ec.europa.eu/economy_finance/international/forums/index_en.htm](http://ec.europa.eu/economy_finance/international/forums/index_en.htm).

\(^{22}\) For more on this, see chapter five on EU representation.

\(^{23}\) Macaj and Nicolaidis, 2014, p. 1071.
best option. Consider, for example, that homogenizing diverging opinions takes much time and energy, and is often seen as a success in itself. Furthermore, the pursuit of one voice can reinforce perceptions of bullying, thereby complicating negotiations or interactions with the EU. Finally, in institutions with a ‘one-country, one-vote system’ – such as the WTO and the G20 – having a numerical advantage makes for significant power in itself.

That being said, considering the ongoing competition among EU member states for Beijing’s economic favour and with antipathy against (too) many European seats on the multilateral negotiating table on the rise, the case for greater coordination and cooperation in EU–China relations appears to be strong. More than in other areas, the EU has shown itself to be capable of getting China out of its comfort zone in the trade field, where the EU has competence and the European Commission speaks on behalf of all EU member states.

Table 1 illustrates not only the different forms of membership of EU member states in global economic governance. It also, and quite literally, unveils the gaps (illustrated by the empty boxes in the table) in this regard. That is to say, it shows where the EU is not represented. In addition, it exposes the diversity of actors – and number of actors – that make up the composite foreign policy actor of the EU in the various settings.

At the same time, Table 1 lays bare the evident fact that different EU member states participate in different settings. What stands out is the fact that most, or a significant number, of EU member states participate in traditional Bretton Woods institutions, while this is not the case in Asian institutions or networks. This is a simple illustration of how the interests of EU member states are divergent, thus also pointing to a challenge involved in preparing a joint framework involving all EU member states. This, in turn, suggests the difficulty of formulating a comprehensive EU–China approach, based on a shared framework that is understood and respected by all players. Another striking fact that appears from Table 1 is the fact that the European External Action Service (EEAS) is mentioned only once. This shows that reality is a far cry from the Commission’s call that, as a general rule of thumb, the EU’s diplomatic service should be the EU’s key organ for the EU’s foreign policy.

While discussing the diversity of objectives pursued by Beijing through its activism in global economic governance, the following chapters elucidate in greater detail also the roles and representation of various European actors in various settings. This is a prerequisite to our final assessment of which (combination of) negotiating strategies and actors are likely to contribute to furthering European interests in specific settings of global economic governance.

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24 For more on this, see Van Schaik, 2013; and Da Conceição-Heldt and Meunier, 2014.
A first and perhaps most obvious challenge that China poses for the EU and its member states in the field of global economic governance concerns its attempts to reform existing institutions. In the traditional system of international politics and economics, Beijing is calling for institutional reform and is using its membership, or non-membership, to expand its influence in global economic governance. These processes are most apparent in the World Bank, the IMF, the ADB, the WTO, the G20 and the OECD.

The best known institutions of global economic governance are the World Bank and the IMF, which together formally form the Bretton Woods system. This system, which was established after the Second World War to regulate economic and monetary issues, has traditionally been dominated by Western European countries and the United States. The World Bank fights poverty and promotes ‘shared prosperity’ by providing grants, (concessional) loans and other support. The IMF functions as a lender of last resort. Together with the Bretton Woods institutions, either Western European countries or a likeminded country such as Japan also largely run the OECD and the ADB.

A less formal institution with a ‘one-country, one-vote’ system, the G20 grants more power to challenger countries, including China. Nonetheless, the established economies have a numerical advantage that still gives them significant power. The WTO has the same voting system, granting each country one vote. However, also here the expertise, manpower and financial might of the developed countries often help them to prevail.

This chapter assesses China’s activism in these Bretton Woods institutions and other organizations that are led by developed countries, and gauges its impact on Europe. The discussion is structured along three key goals that Beijing seeks to promote, namely to: (1) strengthen China’s influence in economic governance – in this chapter, by propagating the need to enhance the legitimacy, role and relevance of existing institutions; (2) employ foreign policy and international politics to further domestic goals – that is, to maintain and increase the domestic legitimacy of the Chinese Communist Party (CCP); and (3) change the rules of the game of international politics and economics, and to promote acceptance of new standards, in an effort to further the interests of China’s foreign policy and diplomacy abroad.
China’s Dual Approach: Engagement and Reform

The government of the People’s Republic of China assumed responsibility for China’s relations with the IMF and the World Bank in 1980, taking over from Taiwan, which had represented China since 1945. The World Bank has arguably been the most important international financial institution for China, which has been the Bank’s fourth largest recipient of loans.\(^{26}\) China has also benefited significantly from its membership of the Asian Development Bank, of which it has become the second-largest borrower after joining in 1986.\(^{27}\) Additionally, after more than 15 years of fierce negotiations China joined the WTO in 2001.

China marked the twentieth anniversary of its history of cooperation with the OECD in 2015. Beijing continues to resist becoming a member of this traditional club, however, which according to some is losing its relevance as emerging countries develop. The Chinese government also resisted invitations to join the (then) G8 (Group of Eight industrialized nations), in doing so indirectly contributing to the creation of the G20 in 1999, a more inclusive forum for discussions about global economic policy, and where China is better able to wield influence.\(^{28}\) Although not often recognized as such, the creation of this new G20 forum – as opposed to an expansion of the G8 – constituted an early success of the Chinese government in reforming the system of global economic governance.

While engaging with them, the Chinese government has also been an active promoter of reforms in the World Bank and IMF. Beijing’s increased activism is seen in China’s increased use of the WTO’s Dispute Settlement Body (DSB), its lobbying to get Chinese nationals in high-level positions in the ADB, and its wide engagement with the G20, which it will chair in 2016. China’s increased participation in global affairs has even influenced the OECD’s DAC, of which it is not a member, for example by promoting trade and investment-based development assistance.

A key goal of the Chinese government in the existing organizations is to gain more influence, so as to be better able to promote policies that conform to Chinese interests. As China’s economic power grows, so do the domestic expectations that this will be recognized in the form of increased influence in multilateral institutions. This aim

\(^{26}\) The three largest (in order) are India, Brazil and Mexico; see World Bank, 2013.

\(^{27}\) Different from most other multilateral organizations, the ADB resisted pressure from the Chinese government to expel Taiwan, which is a founding member of the bank. When China joined the ADB, Taiwan remained, albeit with the altered designation of Taipei, China.

\(^{28}\) The G20 is composed of the traditional G8 members – Canada, France, Germany, Italy, Japan, the United Kingdom, the United States and the European Union – plus Australia, Argentina, Brazil, China, India, Indonesia, Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa and Turkey.
for more influence also relates to the remaining two strategic goals that China is pursuing – namely, using multilateralism as a push factor for domestic reforms, and setting and exporting new standards in areas such as government procurement, debt sustainability and capital account policy.

(1) Strengthening Influence in Economic Governance

Voting Reform and Staffing

The most evident way in which China tries to win influence for itself is through pushing for voting reforms in institutions such as the World Bank and the IMF. As the major power and the largest economy, the United States still has a share of the vote that effectively grants it veto power in these stalwarts of the Bretton Woods system. Behind the United States, the countries with the highest voting share are mostly European. This has led to criticism of the voting distribution in the World Bank and the IMF from China and other emerging and developing countries.

Figure 1 World Bank: Voting Share vs. 2014 GDP Share

![Graph showing World Bank: Voting Share vs. 2014 GDP Share]

Voting Share in World Bank as % of total

GDP (at PPP) share as % of world total


30 Figures 1, 3 and 4 present shares of world GDP in 2014 at purchasing power parity (PPP). In real terms, China’s economy in 2014 was estimated to be US$ 10.4 trillion, ranking second after that of the United States, estimated to be US$ 17.4 trillion (World Bank data).
Europe’s Response to China’s Activism | Clingendael Report, October 2015

The World Bank loans that have been granted to China have greatly contributed to its rapid development. As a result of this history, China is generally very positive about its interactions with the World Bank. However, the Chinese – along with other emerging and developing countries – strongly advocated for the 2010 ‘voice reform’ of the World Bank, including through the G20. These reforms were implemented in 2010 in an attempt to make the share of voting rights between the developed and developing countries more equal. Although China was a main beneficiary of this reform, in terms of voting shares, the Europeans and Americans still dominate.

Figure 1 shows how voting shares are divided compared to a country’s share of global GDP. While one might argue from these figures that the reforms failed altogether, the voting share in comparison to contributions to the World Bank’s funds (depicted in Figure 2) suggest a different conclusion. Former Dutch Minister for Foreign Trade Frank Heemskerk, who is now an executive director at the World Bank, has also lamented the relatively small amount of China’s contributions to the World Bank’s funds.31

Figure 2  World Bank: Voting Share vs. Paid in Contributions to World Bank Funds since 2006

![Voting Share vs. Contributions to World Bank Funds](image)

- Contributions to World Bank funds since 2006 ($ bln)
- Voting share in World Bank as % of total

Source: World Bank, 2015; World Bank, Country Summaries.32


32 Total contributions since 2006 calculated by the authors on the basis of World Bank country summaries, see: [https://finances.worldbank.org/countries](https://finances.worldbank.org/countries). Paid in contributions of Brazil, China and India amount to roughly US$ 93 million, US$ 96 million and US$ 77 million, respectively.
Reforms similar to those for the World Bank were negotiated for the IMF and agreed upon in 2010. This restructuring, however, has yet to be implemented. Reforming the IMF requires approval from national governments of all the members, and the US Congress is still holding the 2010 package back. This lack of progress has strengthened China’s and other developing countries’ belief that the IMF is an institution by the West and for the West.

**Figure 3  IMF: Voting Share vs. 2014 GDP Share**

![Figure 3 IMF: Voting Share vs. 2014 GDP Share](image)

*Source: IMF, 2015; Quandl, 2015.*

Figure 3 shows a comparison between the voting share and the 2013 GDP of a selection of developed and emerging countries. While some countries are relatively accurately represented – such as the United States, India and Brazil – it is clear that all European countries are overrepresented. China is heavily underrepresented as compared to the size of its GDP. The proposed reforms would change this situation slightly, but by nowhere near enough to create truly proportional representation (see Figure 4).

The reforms at the IMF centred on the quota system by which voting shares are determined. The formula used for this system is often criticized because it favours European countries. The target for most criticism is the measure for integration into the global economy, which is calculated by imports and exports relative to GDP. Europe’s single market naturally bolsters this figure for European countries, as it facilitates and increases cross-border trade between EU member states. This is, and will continue to be, the main sticking point of reforms at the IMF.
China's efforts to reform the IMF deserve some consideration, since its efforts are not as unidirectional as is sometimes suggested. Somewhat surprisingly, Beijing fought to keep its share just below that of Japan during the previous quota review.\textsuperscript{33} China likely did not want to be the largest shareholder after the United States and to have to shoulder the responsibilities that come with such a position. This could have made it difficult for China to fulfil its role as leader of the world's developing countries. The Chinese government, at least for now, believes that its interests are better served by not being the IMF's second biggest shareholder.

China can thus continue to use the situation in the IMF defensively, lamenting the poor representation of developing countries. If China was the second largest shareholder, there would be more pressure for it to act offensively in promoting the rights of developing countries, which may not always be in China's interests. As the largest and most advanced developing country in the world, China's ambitions do not always align with those of other developing countries. Furthermore, as China is attempting to make the transition from an export- and investment-driven economy to a consumer-driven economy, its policy wishes will begin to resemble those of developed countries, rather

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\textsuperscript{33} Beattie, 2014.
than developing countries. China’s interests are often best served when it can stay ambivalent about its position.

**Reform of the SDR Currency Basket**

Besides seeking reforms in the voting share of the IMF, China is also trying to get its currency – the renminbi – into the institution’s basket of the Special Drawing Rights (SDR). 34 During the previous SDR review in 2010, the Chinese lobbyed hard for the inclusion of the renminbi. The IMF, however, rejected this request on the grounds that the renminbi was subject to capital controls, was not yet traded enough and was subject to an undervalued exchange rate. 35

With the next review of the SDR coming up in late 2015, China is again calling for the renminbi’s inclusion in the basket. Christine Lagarde, Managing Director at the IMF, has stated that the inclusion of China’s currency depends on the change that China makes in terms of its capital account. 36 Ironically, one of the reasons for not including the renminbi is that this would cause the US dollar to be too influential within the basket. There are fears that the renminbi’s unofficial peg to the US dollar would destabilize the basket.

Additionally, China’s financial policies are not yet of the standard required for a currency to be included. David Dollar of Brookings Institution believes the renminbi currency is far from being freely usable, noting that ‘a big asset-management firm can’t just suddenly decide to take a big position in Chinese yuan, and buy Chinese government bonds. That’s all highly restricted’. 37 Within China, there are two opposing camps: those with business interests who would prefer liberalization; and those who prefer continued state control over the economy. 38 As evidenced by the Chinese government’s interventionist reaction to the issues with the stock market and the decision to devalue the renminbi during summer 2015, this battle is still in full swing.

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34 The SDR have long passed the original purpose for which they were created and are now not hugely relevant in the running of the global economy. The SDR make up less than 4 per cent of global non-gold foreign exchange reserves. Nonetheless, they endure as a status symbol, and occasionally they are used for valuing goods.

35 Rodríguez, 2015.

36 Graham and Yukhananov, 2015.

37 Yukhananov, Palmer and Simao, 2015.

38 This internal power struggle has been ongoing since Deng Xiaoping initiated his reform agenda. However, as businesses grow in China, so too will the business interests, and this could see one group winning out over the other.
The inclusion of the renminbi in the SDR is part of China’s strategy to gain influence in global economic governance. Currently, the SDR consists of the US dollar, the euro, the Japanese yen and the British pound. Should the renminbi be included, this would represent a mostly symbolic win for China: denoting international acceptance of its currency on a par with the other world currencies, and at the same time a shift in long-existing standards of international finance. The decision to include the renminbi would primarily be a political decision and not economic. This is all the more so, because inclusion of the renminbi would have little economic effect; there are no particular economic benefits for the world or China if the renminbi is included in the SDR basket.

China’s appeals are based on the fact that the renminbi is now the second-most-used currency in global trade finance. In 2013, the renminbi overtook the euro to become the second-most-used currency after the dollar, having surpassed the Japanese yen in 2012. The US dollar still leads by far, however, accounting for roughly 82 per cent of the share of global trade finance. This compares with a mere 9, 7 and 1 per cent for the renminbi, euro and yen, respectively.39

Looking at it purely from a trade perspective, however, China’s appeals for its currency to be included in the SDR appear premature. As depicted in Figure 5 below, there are several currencies that have far higher shares in world trade and meet the IMF requirements for inclusion in the SDR.40 In 2013, the Chinese renminbi ranked only ninth on this list – lower than the Canadian dollar and the Mexican peso, among others.

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39 All figures are from October 2013, provided by the Society for Worldwide Inter-bank Financial Telecommunication; see http://www.bloomberg.com/news/articles/2013-12-03/yuan-passes-euro-to-be-second-most-used-trade-finance-currency.

40 Horii, 2015, p. 5.
The biggest victory that China could achieve would be if its suggestions for the SDR replacing the US dollar as the global reserve currency come to fruition. The Governor of the People’s Bank of China (PBoC), Zhou Xiaochuan, published an essay in 2009 in which he argued for replacing the US dollar with the SDR as the world’s reserve currency. According to Zhou, ‘the desirable goal of reforming the international monetary system, therefore, is to create an international reserve currency that is disconnected from individual nations and is able to remain stable in the long run, thus removing the inherent deficiencies caused by using credit-based national currencies’.41 Displacing the United States would be a massive symbolic move by the Chinese, and a clear signal of China’s increased power in the international system. Even if this is not expected to happen any time soon, the Chinese government is promoting slow but steady steps in this direction.

The consequences of a stronger role for the renminbi in the international monetary system are unclear and analysts disagree about possible outcomes. Some point to the fact that the dollar’s centrality to global finance gives Washington substantial leverage to press others to conform to US or US-backed sanctions. Clearly, China stands to benefit from a weakening of this tool in Washington’s economic statecraft kit, while it is eager to develop this instrument for its own purposes. Others argue that there would

41 Xiaochuan, 2009, p. 2.
be no noticeable changes. Europe should explore the consequences of this further in order to ensure that whatever development occurs is not at the expense of the interests of European countries. Attention should be given to what is more likely to hurt European ambitions in economic governance, such as an overreliance on the dollar or the weakening of the effectiveness of economic sanctions against, for example, Russia and Iran.

**Agenda-setting Potential: China at the G20**

After the start of the financial crisis in 2008, a decision was made to elevate the importance of the G20 meetings, which – as opposed to the G7 and G8 – include emerging economies. This suited China, as it views the G20 very favourably, and has rejected several informal advances to join the G8. The informal nature of the G20, without the rigid voting system of the IMF and World Bank, allows China to make full use of its economic weight. The G20 has also been referred to as ‘the only global economic governance platform in which the country [China] can operate as a major power’.42

The new, more expansive role of the G20 in the governance of the global economy also includes setting agendas for other multilateral organizations. For instance, the voting reforms of the World Bank and the IMF were discussed at, and to a large extent pushed by, the G20. The ability to determine what is on the agenda of the G20 and therefore what can be pursued in other multilateral bodies is an important power. The 2016 summit of the G20 will be held in China, allowing Beijing to showcase its ideas to the world for the near and longer-term future of the global economy. Possible topics include the 2010 IMF reforms, renewed focus on global trade negotiations at the WTO, and presenting infrastructure projects that can be taken up by the new development banks established by China.

The increasingly introverted nature of the United States and Europe has given China an opportunity to increase its influence in global economic governance. As evidenced by the IMF reforms, American politics are stuck in a stalemate; the United States is no longer capable or willing to take the lead in all international matters. In Europe, on the other hand, the Greek crisis and the immigration debate have focused most of the attention on internal issues. This has left the door open for China to step up and demand a larger role in the governing of the global economy. Taken together with China’s leadership of the 2016 G20 summit, Beijing now has an excellent opportunity to push forward its own agenda for global economic governance.

42 He, 2014, p. 6.
(2) Furthering Domestic Goals

Engaging and Challenging the WTO

An early example of China’s use of multilateralism for domestic reforms was its accession to the WTO in 2001. In order to qualify for membership, China was forced to agree to an unprecedented list of concessions. The agreed terms stretched from topics such as market access and transparency to intellectual property rights and government procurements. This list was a useful tool for the pro-reform camp in China to push through economic reforms. Although not all of these concessions have been met in practice, there have undoubtedly been changes in most of China’s economic policies.

China has, on the whole, changed significantly since its accession to the WTO. The closed off and centrally driven economy that was China in the pre-Deng Xiaoping era had already changed before 2001. The extra pressure of WTO membership, however, and the benefits that WTO membership promised, strengthened the case for further reforms. Nonetheless, China has not completely adopted the standards that Europe had hoped that it would. Hovering somewhere between the two extremes – that of China pre-WTO accession and a completely market-economy China – says a lot about the larger debates around China’s rise and its multilateralism. This illustrates the general trend that the Chinese government is not converging on the status quo, nor is it destroying or replacing the existing system. Rather, it is trying to alter the system to fit its strengths and needs.

In the area of intellectual property rights (IPR), a traditionally weak aspect of China’s legal system, a kind of knock-on effect is taking place. The domestic reforms pushed through because of the WTO accession are beginning to cause natural domestic pressure. Chinese companies are now beginning to innovate and create products that require protection through IPR. These companies are putting domestic pressure on the Chinese government to reform the IPR system. This is linked to China moving up the global value chain.

2016 will be an important year for China’s relationship with the WTO, as its status as a non-market-economy country will come into question. The fifteen-year period during which China agreed not to be considered a market economy will then end. This can have serious consequences on anti-dumping cases brought against Chinese companies. As a non-market economy, the burden of proof – that is, for showing that market-economy conditions prevail in an industry in question – lies with the Chinese, and other countries are free to use alternative pricing methods for Chinese goods.

It is for now uncertain what will happen when the fifteen-year period comes to an end in 2016. EU Trade Commissioner Cecilia Malmström has stated that she does not believe
that China automatically qualifies as a market economy when the term expires.⁴³ Treating China as a market economy would furthermore take away a potential carrot for further reforms and would legitimize the Chinese style of running an economy. On the other hand, some argue that a more constructive approach, in which China is treated as a market economy, could be more welcoming and effective.⁴⁴

**Market-oriented SOE Reforms**

The collaboration between China and the World Bank on the *China 2030* report, which was released in 2013, can also partly be seen as the use of multilateralism for domestic reforms. The purpose was to ‘prepare a strategic framework for reforms’ that could then be implemented in China.⁴⁵ The commissioning of this report by China’s Communist Party shows its wish to legitimize certain calls for reform. A central focus of the report was reform of state-owned enterprises (SOEs) in China. Although calling for changes in the SOE system, the report did allow for seven sectors over which the Chinese government would keep ‘absolute control’.⁴⁶

Other areas where the World Bank’s *China 2030* report suggests reforms are the financial system with relation to obtaining capital, land and agriculture, and the labour market. The suggested financial reforms would involve the liberalization of capital. Looking at the reforms taking place in China today, they largely follow the big trends of the *China 2030* report. The Silk Road initiatives, which aim for more development in the western regions, and experiments with the *hukou* household registration system⁴⁷ reform, are two examples of this. The shape and extent of reforms in China will largely determine the possibilities for European countries and the EU in their relations with China.

China’s use of multilateralism to legitimize or increase backing for domestic reforms should be seen as a positive sign for Europeans. Multilateral organizations offer European countries opportunities for dialogue with China. Keeping in mind that China is also attempting to set new standards, the best way to ensure alignment with European standards or wishes is through dialogue with China. If China shows that it is willing to use multilateral organizations to lock in domestic reforms, this is an avenue through which Europe can influence the direction of China’s development.

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⁴³ Dalton, 2014.
⁴⁵ World Bank, 2013.
⁴⁶ These seven sectors are: defence; electricity generation and distribution; petroleum and petrochemicals; telecommunications; coal; civil aviation; and waterway transportation. See World Bank, 2012, p. 26.
⁴⁷ The *hukou* housing registration system determines a citizen’s right to live and work in a city and have the benefits that come with that, such as healthcare, education and other government services.
(3) Promoting Acceptance of New Standards

Adding Pressure to Reform by Creating Alternatives

China’s decision to pump billions into two new institutions, the NDB and the AIIB, are a clear statement of intent to set new standards in the field of multilateral development banks. After all, this money could also have gone to the World Bank and ADB, which fulfil the same kind of role that China hopes the NDB and AIIB will. As will be elaborated in the next chapter of this report, the decision to create new institutions shows that there are aspects of the existing institutions with which China is not content. The new organizations offer China a platform to set and export new standards in government procurement, debt sustainability, and environmental and labour conditions.

The World Bank and ADB are often criticized for not doing enough to address the infrastructure gap in Asia. A 2009 report by the ADB calculated that between 2010 and 2020, some US$ 8 trillion would be needed to close the infrastructure gap in the region.\(^{48}\) The World Bank and the ADB both finance projects that address this issue, even if their activities – as well as those of individual countries that are active in the region – are said to be ‘a drop in the bucket’. One important reason for this is lack of capital for funding. In addition, filling identified gaps requires multi-step projects and is thus, inevitably, a long-term process. Finally, upholding the standards of these banks means that much time goes into preparing, structuring and placing projects in the market.

The creation of the AIIB is therefore in a sense timely, as it addresses a burning need in Asia. However, the decision by China to put its capital into this new bank rather than in the existing institutions reveals Beijing’s desire to create a bank that better suits its own interests. This includes a different understanding of how to run the bank, as well as of how to unfold the bank’s activities. Beijing considers the World Bank and the ADB to be ineffective at solving issues in the Asian region. In placing its capital in the AIIB rather than the World Bank or ADB, China suggests that it believes the AIIB will be better equipped at solving Asia’s infrastructure problem.

Should these new multilateral development banks (MDBs) operate differently, this will be an example of the exporting of new ‘Chinese’ standards. While recognizing that certain long-held practices may be improved based on the insights of China and other countries, there is a risk that the various MDBs will engage in a race to the bottom in terms of projects of choice as well as standards. China’s stance on government procurements, labour and environmental standards, and debt sustainability is of particular concern in this case.

\(^{48}\) ADB and ADB Institute 2009, pp. 4 and 10.
Promoting a ‘Chinese’ Understanding of Trade Policy Rules

China’s acceptance of the various terms required for its WTO accession was a signal that China was serious about reform. Since then, plenty of legislation has been passed. Enforcement of this legislation is less impressive, however, and is rather inconsistent and insufficient. Five areas of concern are often mentioned: first, China’s adherence (or lack thereof) to IPR; second, the technical barriers to trade; third, conformity to an open market; fourth, the government’s procurement procedures; and finally, following through on trade-related investment measures and commitments.49

China’s increasing influence in economic governance and its desire to forge its own path have led to a situation in which the current post-war system is being challenged. One consequence of this could be the normalization of a ‘Chinese’ understanding of IPR. The Chinese have long had lax rules in this field, in order to enable Chinese businesses to catch up in terms of technological development. However, this has led to a widespread cultural belief that IPR boundaries are suggestions rather than laws and that infringements will not be punished. According to Europol, over two-thirds of the total amount of counterfeit goods in the EU originates in China.50

The continued presence of the SOEs not only contributed to China’s rapid development, but has also become an example of China’s new standards. The system has created behemoths of industry: massive SOEs that occupy monopoly positions. These SOEs are generally profitable businesses, but their monopoly positions hinder the development of China’s private sector and provide unfair competition for foreign companies. The annual survey by the EU chamber of commerce in China illustrates that European businesses increasingly find that the reforms made by the Chinese government in the area of rule of law and fair competition are lacking. A majority of European companies surveyed for this report perceive that they and their fellow foreign invested enterprises in China ‘receive unfavourable treatment compared to their domestic Chinese counterparts’.51 These issues encountered by foreign businesses in China, the weak rule of law and unfair government backing of Chinese companies are more examples of the standards that China is attempting to normalize in global economic governance.

To sum up, China’s unwillingness to reform completely its economy and its trade policy to conform to Western and WTO standards indicates that new standards are being set in this area too. China’s success in setting these new standards would signal to other countries that the WTO’s standards are not set in stone, can be altered and may on some occasions be loosely interpreted. So far, European countries have

49 Blanchard, 2013, p. 250.
50 Europol, 2015.
51 European Chamber, 2015, p. 38.
upheld the high standards because of their belief that a world conforming to the WTO’s standards is better for everyone. China itself has also benefited hugely, and still benefits, from this rules-based trading system and from the open economies of other countries. However, when countries decide that a less liberal approach is acceptable, this will be particularly painful for those countries that already have open economies. In addition, the greater diversity of interpretations of WTO regulations will stir trade disputes – or even trade wars. To challenge certain fundamentals of the existing system is to create new dynamics that even China may not be able to control and from which it likely stands to lose – for example, if investors pull out from China because of its uncertain, politically influenced investment climate, or if calls demanding reciprocity gain strength in developed countries, including in Europe. Signs of both developments are already apparent.

Amending IMF Standards

The inclusion of the renminbi in the SDR without it matching long-standing requirements set by the IMF would signal the acceptance that IMF rules are open to discussion. The push to include China’s currency in this basket of symbolic importance is a clear statement that Beijing disagrees with the current criteria. Moreover, it is illustrative of China’s growing capacity to push its standards onto the current multilateral system and its rules and regulations, in this case in the form of capital account liberalization and fixed exchange rates.

The reasoning behind the IMF’s current position on the issue of capital account liberalization is based on the fact that, for most industrial economies, it has been beneficial and healthier to be more integrated. Furthermore, in theory, the liberalized capital accounts are meant to allow for a more efficient distribution of capital. In this way, money can flow from capital-rich countries to capital-poor countries, leading to widespread development.

The push by China for the renminbi to be included in the SDR despite being unofficially pegged to the dollar and the capital account not being liberalized suggests that it is not certain whether China is planning on ever completing this process. As with the market economy status at the WTO, the promise of the renminbi’s inclusion in the SDR can be used as an incentive to influence China’s policies in a direction that is more beneficial for Europe. Capital account liberalization would facilitate better access to the Chinese market, which is one of the main areas in which Europe is lacking in its economic relations with China.

During the previous SDR review, the United States and European countries stopped the renminbi from being included. The United States alone has the votes to veto any decision on this matter. Nevertheless, European backing for the renminbi’s inclusion would signal a readiness to adjust long-standing IMF standards significantly.
ODA Definition Evolving

The OECD’s DAC has for decades set the standards for what can be counted as official development assistance (ODA) for all OECD members. China has not joined the OECD DAC and a significant part of its efforts in this field do not meet the criteria for ODA status. For instance, Chinese development cooperation efforts involve a greater loan element than the traditional ODA definition. In addition, they are closely aligned with domestic objectives such as trade and investment promotion and energy security, and include an element of military assistance. Most Chinese projects focus on infrastructure and promote economic development. These projects are almost always awarded to Chinese companies, which conflicts with the government procurement standards for ODA.

In a sense, divergent interpretations of development assistance are not new; similar differences in conceptualization and practice of development assistance have existed between the OECD and some of its Asian members, especially Japan. China’s strong economic and financial weight is now shifting the balance and forcing change upon the OECD, which it did not feel the need for in previous decades.

The Chinese government has developed its own view of ‘what constitutes foreign aid and what qualifies as “external assistance”.’ It has become a significant player in the field of bilateral lending, with similar numbers reported for the period 2010–2012 as the Netherlands. The increased presence of China has created tension between the OECD’s standards and practices and those of China.

It is difficult to compare accurately the Chinese statistics on development assistance with OECD data, because the Chinese use different calculations – as well as differing conceptualizations. With its distinct approach to development assistance, China is providing competition to other large lending countries, such as the members of the OECD DAC. Developing countries can increasingly choose between donors and their varying conditions and standards. In this type of system, there is the same potential as with development banks that standards and conditions are gradually adjusted to keep up with, or ahead of, the competition. Government backing of Chinese companies that

52 There are various norms for meeting the criteria of ODA relating to: (a) transparency; (b) tied aid and export credits; (c) social and environmental protections; (d) corruption and governance; and (e) the management of debt; see Bräutigam, 2010, p. 11.


54 The second White Paper on Foreign Aid, which was released in 2014, revealed that between 2010 and 2012, the Chinese government spent US$ 14.41 billion on development assistance. By comparison, over the same period the Netherlands spent US$ 18.49 billion on ODA. See 2015 OECD data for Netherlands ODA https://data.oecd.org/oda/net-oda.htm.
have laxer labour and environmental standards makes Chinese development cooperation more attractive to certain recipient countries that prefer quick projects without too much paperwork or too many conditions.

The OECD DAC has responded to the increased Chinese activity in development assistance by creating the China–DAC study group. This group was created in 2009 to promote dialogue between Chinese officials and OECD member state officials on the topic of development assistance. The group examines and discusses the experiences of DAC members and China in terms of successful and unsuccessful development assistance strategies. China is interesting in this sense, because it has extensive domestic experience with how to use assistance for rapid development. However, it has less experience as a lender and is following a different path than that of the DAC. To the extent that the study group constituted an attempt by the DAC to invite the Chinese to follow its ODA standards, it appears to have been largely unsuccessful, for while displaying a willingness to learn and adjust to the extent that it suits its own standards, the Chinese government is hardly conforming to OECD standards. In fact, quite the opposite is happening: the ODA definition is being reviewed – and it is not unlikely that it will include certain military activities in the future – and European countries are increasingly turning to the economic approach themselves.

Implications for Europe: The EU and its Member States

The steady growth of China’s economy and its influence in the world have resulted in increased activity in the existing institutional infrastructure. Whether China is seeking to increase its influence, push through domestic reforms or to export new standards, the Chinese presence is felt throughout most major multilateral organizations.

Although these long-term processes are hardly new to those directly involved, the combined effects remain little understood – especially in Europe, where governance is more dispersed than in any one specific country. As proponents of effective multilateralism, European countries are directly affected by many of China’s actions in this field. The implications for Europe can be divided into three categories: the loss of direct influence; increased challenges to maintaining a level playing field; and greater competition resulting in an altering of standards that took European countries decades to develop.

Losing Influence or the Onset of Irrelevance

In the institutions led by developed countries, European policy-makers essentially face a choice between three options. One option is to continue the reforms and accept the resulting loss of influence; the second option is to block or obstruct new attempts at reform and to risk making the existing institutions irrelevant; while the final, and in
the long term most beneficial, option would be to use the remaining influence in the existing institutions to ensure a strong and sustainable position for EU member states in the future.

The voting reforms in both the IMF and the World Bank are evidence that the need for change is catching on in the West. However, as with any country, European leaders want to maximize their influence, including through multilateral institutions. The European countries have all ratified the most recent IMF reforms, showing that they believe a stronger voice for the developing world is important. Furthermore, some countries believe that they should not give up their power before they can ensure that proper reforms will be passed.\(^5\) This probably stems from the realization that continuing to block or delay reforms of the existing institutions will damage their legitimacy in the eyes of the developing world.

In the case of the IMF, the EU member states could use their current influence to reform the IMF in such a way that voting shares are more equal but that the representation of the European countries is better than it currently is. How this can be achieved is still up for debate, but one option being explored is a common ‘Eurogroup’ constituency for the Eurozone countries. This would ensure that Eurozone members act on the basis of a common framework. At the same time, this would show that the Bretton Woods institutions are serious about giving the developing world a proper voice.

There is already widespread talk about the ‘Western hegemony’ over international institutions and this will only be reinforced if reforms are no longer pursued or offered as a serious possibility. This raises the risk that the Bretton Woods institutions can lose their relevance as developing countries no longer believe in them. With China creating parallel institutions, this danger looms larger than ever. Alternative organizations offer developing countries new routes to achieve similar goals.

European countries should be careful that the creation of parallel institutions does not result in stalling or decreasing Chinese and developing countries’ participation in the existing institutions. In this regard, the decision by numerous European capitals to join the AIIB should be seen as positive, as they set a good example by showing commitment to various avenues of multilateralism. The creation of parallel institutions appears to serve Chinese interests that are beyond the institutions themselves. This includes furthering specific Chinese foreign policy initiatives – in particular ‘One Belt, One Road’ – that also aim to strengthen partnerships and stability in regions that are of particular importance to Beijing. While this may be only natural for an emerging power, European countries would do well to continue to remind the Chinese and others of this reality.

\(^5\) Authors’ interview with a representative from the Dutch Ministry of Foreign Affairs, July 2015.
Level the Playing Field

The World Bank’s *China 2030* report and the trade and economic policies being pursued by China point to another important implication for Europe of China’s activities in global economic governance. The SOE system was specifically pointed out as an area in need of reform. Although the SOEs have undergone some reforms since the 1980s, they still leave much to be desired: while many smaller SOEs have disappeared, the big SOEs – mainly those involved in the production and distribution of natural resources, materials and energy – have only gained in strength. As the aforementioned European Chamber report attests, the European companies that operate in China often still find that they are in an unfair position compared to many Chinese SOEs.56

The seven industries over which the Chinese government wants to keep absolute control57 are another example of the unfair competition to which foreign companies are exposed. This should be an important consideration for European countries when they evaluate their relations with China. The general wisdom is that companies need to be involved in China so as to benefit from the eventual rebalance of the Chinese economy to more consumer-driven growth. However, if there is no indication that reforms are on the horizon, the tension between having a presence in the Chinese market and being able to compete fairly in this market will not disappear.

In terms of market conditions and fair competition, the European market is open in most sectors. When other countries, especially an influential country such as China, openly support their SOEs and fail to enforce fully the WTO’s regulations, this can become problematic for European countries. The Chinese style of IPR enforcement, for instance, can either prevent European companies from investing in China, or it can cause them to lose their technology. Special consideration should be given to the implications that this has on European economic and business interests in China. Taken together with the other implications for Europe that are discussed in this report – the loss of influence and the possible consequences of increasingly accepted views on the Chinese government’s backing of domestic companies and China’s fragile rule of law – this can significantly weaken Europe’s position in the international system.

Towards a ‘Low-cost International Order’?

China’s promotion of its own version of economic policies – towards the capital account and government intervention in the market, government procurement and environmental

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56 European Chamber, 2015.
57 As noted above in footnote 44, these seven industries are: defence; electricity generation and distribution; petroleum and petrochemicals; telecommunications; coal; civil aviation; and waterway transportation. See World Bank, 2013.
and labour standards that govern the global economy – is another area that can have far-reaching implications for Europe. The standards that govern the Bretton Woods institutions, the WTO and development assistance largely stem from the European and American traditions that – notwithstanding differences between them – share a belief in neo-liberal political and economic standards. China’s actions in the various existing institutions aim, at least in part, to alter the standards and practices of the existing system to fit its own needs and strengths better. While there is room for improvement in the existing standards, some of the ideas that are discernible from the Chinese actions would be a clear step back from existing liberal political and economic standards.

The standards that European countries have developed over the years through trial and error, and for which they have fought hard, are now in danger of being pulled back in some areas. For instance, the Chinese standards in government procurement are lower and more susceptible to corruption. This should be of serious concern for Europe and other countries that actively aim for standards that promote openness, transparency and a level playing field. Furthermore, this can harm the developmental progress of developing countries. Thought should be given to how European countries can best counteract a degrading of the standards as a result of increased Chinese influence in certain fields of global economic governance.
3 Towards a Sino-centric Financial System?

As well as challenging the existing institutional architecture, China is reshaping the international political and economic system indirectly, by establishing alternative institutions and networks. The Chinese government has played a key role in recent years in the creation of three multilateral financial institutions, in what some see as an attempt to rival the Western-dominated system of global economic governance and to create a Sino-centric financial system. These new cooperative mechanisms are the AIIB; the NDB, which is also known as the BRICS bank; and the CRA, a BRICS-initiated alternative to the IMF. In addition, the Chinese have proposed creating a development bank of the Shanghai Cooperation Organization (SCO), a six-country Eurasian security, political and economic grouping that is dominated by China and Russia.

Considering the mix of economic, political and geostrategic goals promoted by Beijing, what is the right balance for European countries in engaging with China on these new institutions, yet without overly accommodating it? How do Chinese initiatives to create new institutions in the field of global economic governance impact on European interests and Europe’s ability to promote its interests in the international system of global governance? How can European capitals best represent their interests in the AIIB and in relation to other new institutions, and what influence can they expect to have on the style and operations of these organizations?

This chapter analyses how the creation by China of institutions that are parallel to the Bretton Woods system impacts upon Europe. It does so by discussing how China’s activism contributes to the three aforementioned main goals that Beijing seeks to promote, and by assessing how this relates to European interests. The analysis will focus on the AIIB, NDB and the currency pool that were established in mid-2015 and that are expected to begin operations from late 2015. The SCO development bank is at a much earlier phase of development and may never become reality, and so will not be considered in detail here. Moreover, China’s interest in the SCO development bank seems to have cooled recently, following Russian opposition. This initiative has been surpassed by the successful creation of the NDB and especially the AIIB, which aim to fulfil the same task of infrastructure development.

58 More recently, Russia is seen to be giving way to China in the BRICS and SCO frameworks, as the Chinese are skilfully subsuming the Russian-led Eurasian Economic Union into their wider Silk Road initiative; see http://www.lowyinterpreter.org/post/2015/07/17/Russia-gives-way-to-China-in-BRICS-and-SCO.aspx.
2015: A Year of Breakthroughs

The creation in June 2015 of the China-led AIIB, with 57 founding members including fourteen EU member states, signified a breakthrough in global economic governance. For the first time in more than seven decades, a multilateral bank with membership covering all continents was established. The enthusiasm with which European and other developed countries decided to join the Bank in March 2015 surprised many – not only the United States and Japan, which decided to stay out, but also Beijing itself.

The AIIB’s broad multilateral representation now makes it China’s priority project and is also the reason why this bank constitutes the primary challenge to the existing institutions. By comparison, the launch in July 2015 by the BRICS countries of the NDB, as well as of the CRA, was lower in profile and received far less attention, from political leaders and in the international media. This difference is certainly not explained by the size of the initiatives, for both BRICS initiatives – like the AIIB – are set to encompass a total capital of US$ 100 billion.

For its part, the currency reserve pool is meant to contribute to financial stability in much the same way as the IMF’s SDR does – that is, by offering short-term financial assistance to the central banks of BRICS nations that they can draw on when one of them suffers a shortage of dollar liquidity. The BRICS agreed to create this fund in 2013, after seeing investors pull money away from emerging economies, causing their currencies to weaken.

The AIIB and the NDB – as well as China’s Silk Road Fund59 – share similar missions but differ in the targeted market. Each aims to accelerate infrastructure construction projects to improve connections with neighbouring countries and regions, to spur local industrial upgrading and urbanization, and to pave the way for the (re)construction of two ‘Silk Roads’, over land and by sea.60 The new banks are thus instruments of China’s quest to offer financing capabilities and technical know-how to help itself and other Asian countries develop infrastructure and, thereby, to strengthen their economic capabilities more broadly.

There should be little doubt, however, that the China-led banks aim for more than to spur development in countries along the route by means of infrastructure projects. This is important to European capitals, because while bridge building, road development and improved energy grids may also benefit European companies wanting to do business in the region, other Chinese aims may conflict with European

59 This Chinese initiative will be elaborated upon in the next chapter.
interests. Beijing’s offer of alternatives to established standards of governance and labour rights, for example, weaken fundamental values that took European countries decades to develop. And while the furthering of domestic economic reform in China can be expected to have positive effects also for Europe, it should be regarded with caution, in that it also involves steps away from market-oriented reform. The following paragraphs elucidate this in greater detail.

(1) Strengthening Influence in Economic Governance

Having a Greater Say: Votes, Shares, Personnel

Creation of the AIIB and the NDB was in part a reaction to the position of the BRICS and other emerging countries in the existing institutions. Creating parallel institutions seems beneficial in two ways: by offering real alternatives; and by injecting a greater sense of urgency about the need for reform of traditional institutions. Indeed, as the BRICS nations at their 2015 summit paved the way for the creation of the NDB and the CRA, they also floated the possibility of creating an independent BRICS rating agency and discussed the IMF reform that should give a louder voice to developing countries in decision-making.

Table 2 The 57 Founding Members of the Asian Infrastructure Investment Bank

<table>
<thead>
<tr>
<th>Region</th>
<th>Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asia–Pacific (25)</td>
<td>Australia, Bangladesh, China, India, Kazakhstan, Kyrgyzstan, Maldives, Mongolia, Nepal, New Zealand, Pakistan, Sri Lanka, Republic of Korea, Tajikistan, Uzbekistan</td>
</tr>
<tr>
<td></td>
<td><strong>ASEAN member states:</strong> Brunei, Cambodia, Indonesia, Lao, Malaysia, Myanmar, Philippines, Singapore, Thailand, Vietnam</td>
</tr>
<tr>
<td>Middle East (10)</td>
<td>Egypt, Iran, Israel, Jordan, Kuwait, Oman, Qatar, Saudi Arabia, Turkey, United Arab Emirates</td>
</tr>
<tr>
<td>Europe (20)</td>
<td>Azerbaijan, Georgia, Iceland, Norway, Russia, Switzerland</td>
</tr>
<tr>
<td></td>
<td><strong>EU member states:</strong> Denmark, Poland, Sweden, United Kingdom ** Austria, Finland, France, Germany, Italy, Luxembourg, Malta, Portugal, Spain, The Netherlands</td>
</tr>
<tr>
<td>Latin America (1)</td>
<td>Brazil</td>
</tr>
<tr>
<td>Africa (1)</td>
<td>South Africa</td>
</tr>
</tbody>
</table>

Source: Adapted from the official website of the AIIB (http://aiibank.org/yatouhang_04.html).
China is by far the most influential country in the AIIB. While media reports suggested that China lured the United Kingdom – and thereby other European member states – into the AIIB after expressing its willingness to forego a veto right, the Articles of Agreement give it such a veto in all but name. With slightly more than 26 per cent of voting rights, Beijing has the power to block certain proposals that require a super-majority of at least 75 per cent of the total vote. India holds the second largest share but is a distant second, with 7.5 per cent of voting rights.

Figure 6  AIIB: Distribution of Voting Rights

China: 26.1%
Regional members other than China: 48.9%
Non-regional members: 25%

Regional members: ±75%
- China: 26.1%
- India: 7.5%
- Regional other: 41.4%

Non-regional members: ±25%
- Eurozone countries: ±15%
  The Netherlands: 1.16%
- EU member states other: ±5%
- Non-regional other: ±5%

Source: Ministry of Finance of the Netherlands, 2015.

China is also to play a key role in the daily operations of the AIIB. The AIIB is headquartered in Beijing and its first president, Jin Liqun, is a Chinese national. Furthermore, if the ADB is any indication, the AIIB’s management is likely to be dominated by Chinese nationals and China clearly has significant influence over a substantial number of regional members. This is all the more important as European members will be financially hard-pressed to commission their own nationals. Moreover, the AIIB aims to be ‘lean and mean’ with a non-resident board – following a suggestion of the so-called Zedillo Report, which was commissioned by the World Bank in 2009 – giving the Secretariat a more significant role in daily operations.
In the set-up of the AIIB, including the writings of its Articles of Agreement and procedures, the Chinese government has gone to great lengths to reassure other members of its good intentions. Processes are said to be relatively transparent and (former) advisers of the World Bank and the ADB were asked to prepare draft texts. The Secretariat has reportedly generally taken a quiet approach in meetings, in which European representatives have reportedly been the most vocal. Whether this is (also) symbolic of a more Asian diplomatic style – in which formal meetings are generally about consensus, and deals are made before and after – remains to be seen. In any case, the AIIB shall in due time be judged on its practical undertakings.

Even more so than in the AIIB, which is more of a truly multilateral institution, the sheer size of China’s economy as well as its currency reserves and diplomatic representation result in Beijing having significant sway over the BRICS Bank (or NDB). The Chinese have succeeded in hosting the headquarters of the NDB, which is located in Shanghai. To compensate, the first president will be Indian, the first chairman of the board of governors will be Russian, the first chairman of the board of directors will be Brazilian, while the first regional centre of the NDB will be in South Africa. By sharing the initial capital subscriptions, as well as voting rights, equally among the five founding nations, the BRICS have managed to portray an image of equality. All five members will contribute an equal share of US$ 10 billion to the NDB’s total subscribed capital base. Set against this context, it is unlikely that Beijing will play the key role in further building up the capital base to the projected US$ 100 billion, even if the other BRICS nations are unlikely to be able to contribute substantially more capital in the foreseeable future. In addition, while non-founding members may be invited to join in the future, the total BRICS share is not allowed to decline below 55 per cent.

The strong role played by China relative to the role of other BRICS members is most evident in the currency reserve pool, to which China will contribute more than twice as much as the other members. China has committed US$ 41 billion, giving it the largest share of voting rights at 39.5 per cent. Russia, Brazil and India will each contribute US$ 18 billion, and South Africa the remaining US$ 5 billion. Although substantial, this amount pales in comparison to the IMF’s reserves and would likely not be enough to save even the weakest of the BRICS. This is confirmed by the fact that, under the terms of the CRA, a country can only borrow more than 30 per cent of its allowed maximum if it first requests a monitoring programme at the IMF. The CRA is clearly not yet a serious

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challenge to the existing system of reserve currencies at the IMF; rather, it is an extra measure to ensure further financial stability. As a result, the CRA is currently more of a symbolic move that delivers a primarily psychological blow to the traditional system of global economic governance.

China in the Lead, Balancing its Bets

Beyond enhanced voting power, increasing cooperation among the BRICS nations is deemed to be important, especially by China and Russia, which hope to continue to develop their ties with the other emerging countries. Together, they represent the vocal, activist wing of the BRICS – albeit by China in a more subtle way and Russia rather openly. India is the neutral middle, and Brazil and South Africa are the more likeminded with the Western countries. Such divergence within the BRICS is unbefitting for China and Russia, which wish to present a united front that can compete with the traditional Western powers. This is probably also one of the reasons why the NDB took a relatively long time to become established. Tellingly, the NDB’s website does not look particularly professional, although it improved quite a bit in mid-2015. All of this raises questions about the seriousness of the NDB, which is the most ambitious BRICS undertaking.

That being said, China’s activism in different settings shows that China is serious about enhancing its influence in global economic governance and that it is balancing its bets. China appears to be stepping up its efforts in the multilateral arena because of a ‘positive feedback loop’ – that is to say, following earlier positive experiences with multilateralism, China is now expanding its efforts. What this might suggest for the future is that if these institutions achieve positive results for China, Beijing is likely to advance its activism in the field further. Seen in this perspective, the AIIB and the NDB can be viewed as signs of things to come.

Soften the China Factor, Reduce Malpractice

Having a strong voice within the new institutions, the multilateral guise provides Beijing with a welcome opportunity to diversify its bilateral ties with other countries. On the one hand, going through the AIIB or the NDB can be an opportune way to soften the acrimony that is perceived against Chinese economic intrusion in certain instances. In this sense, investments through the AIIB or NDB – or other existing institutions – offer a way for China to prove that it is still a constructive partner. Concerns about China’s intentions within the broader context of its economic and geopolitical rise are after all not unique to developed economies, but, rather, are shared by certain developing countries in the region, albeit to different extents.

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65 Sohn, 2012, p. 78.
As China began to engage more with other countries in the Asian region and beyond, especially in Africa, it often did so under the guise of a win–win relationship. Beijing – and recipient countries see this – has a more honest stance than that of Western countries. Additionally, the Chinese considered this as necessary to continue China’s economic growth, on which the Party has based its legitimacy. However, China’s massive economic growth and approaching parity of its gross domestic product (GDP) with the United States are making other states worried about China’s actions and ambitions. As evidenced by the rising tensions in the South China Sea, Beijing’s strategic interests are nowadays increasingly at odds with those of its neighbours and Western powers, especially the United States. This has led some to conclude that the ‘Washington consensus’ could become the ‘Beijing dilemma’ – as it is increasingly doubtful that ‘the mutual acquiescence that underlies the current US-led system in international development finance may prove elusive under Chinese management’.66

China’s numerous infrastructure projects all over the world – funded through the China Development Bank and the Export–Import Bank of China – have in certain places incited local resentment. Beijing thus has a growing interest to appease host governments that see Chinese companies overtaking the local economy, and even third countries that are warily following Beijing’s growing activism in economic or development cooperation. Going the multilateral route, Beijing stands a better chance of reducing malpractices by its own corporations.67 Multilateral institutions thereby serve the Chinese interests by softening the fears of Chinese economic dominance, including some of the communal acrimony that is perceived against Chinese economic intrusion.

In certain cases, including when the interests of Beijing and a developing country lie beyond the standards and procedures of one of the multilateral banks, Beijing still has the opportunity to go the bilateral route. This was seen in the case of Pakistan, for example, to which President Xi Jinping pledged a spectacular US$ 45 billion in infrastructure investment in April 2015 under the aegis of the Silk Road initiative.

Finally, the multilateral route is a way in which Beijing can send not just positive messages, but can also signal more negative ones. Indeed, certain Chinese foreign policy strategists have argued that the AIIB should support China’s strategic interests and that countries disrespectful of China should receive less favourable consideration. This has been echoed by officials from various East Asian as well as European countries, who have voiced concerns about being treated unfavourably if their country had opted to stay out of the AIIB. Clearly, the benign character of China’s activism is already under pressure in more than a few capitals, especially in neighbouring countries. Beijing may soon be hard-pressed to fend off accusations that its attempts to reshape the traditional system of global governance to suit its own objectives provide little benefit to (other) developing countries.

67 Zha, 2015, p. 10.
(2) Furthering Domestic Goals

Promoting Chinese Trade and Investment Abroad

In a sense, the establishment of infrastructure funds is a logical step in the Chinese government’s long-term efforts to support the internationalization of its companies. This started with the ‘Go Out policy’, which was initiated in 1999, followed in 2000 by its ‘Go West policy’. While the stimulus package of 2009 and the Silk Road Fund were undertaken by the Chinese government unilaterally, the time was now ripe for multilateral undertakings as well. According to Yun Sun, an expert on Chinese foreign policy at the Stimson Center in Washington DC, there has indeed been pressure to use the AIIB’s loans to ‘advance China’s economic agenda, especially the export of Chinese products and services’. Much the same should be said of the other financial institutions.

In its latest five-year plan, the Chinese government put forward the ‘Strategic Emerging Industries’ initiative. Through this industrial policy, Beijing sets out to promote China’s strength in seven industries, namely: energy saving and environmental protection; new generation information technology; biotechnology; manufacturing of high-end equipment; new energy; new materials; and new energy vehicles. While these industries were subsidized to the tune of several hundred billion US dollars between 2010 and 2015 without being subject to state aid rules, the newly created investment banks will contribute to promoting their activities.

The aim of promoting Chinese exports may not appeal to all partners, however, especially if this is supported by vast government funds. China’s subsidization of these industries gives them an unfair advantage and is at the expense of Europe’s competitive edge in these key sectors. This matters all the more to Europe, as these industries constitute the high valued-added segment of the global economy that has been dominated by developed economies.

Pushing Renminbi Loans?

While it is clear that the China-led financial institutions will facilitate outbound investment, a question that remains is whether this will also result in a stronger presence of the renminbi on the global stage. The internationalization of the Chinese renminbi has gained sway in recent years, driven by increased trade settlement, offshore deposits, central bank currency swaps and issuances of renminbi-denominated bonds.

69 European Political Strategy Centre, 2015, p. 5.
Opinions are divided on whether the new financing mechanisms will contribute to this trend. While some argue that the AIIB will further the internationalization of the Chinese currency, others suggest that this is not necessarily so.\footnote{Zha, 2015, p. 10; and Tu Yonghong, quoted in Zhao, 10 July 2015.} What is beyond much doubt, however, is that the IMF and World Bank contributed to internationalization of the US dollar. Similarly, the AIIB in particular could raise and extend loans in renminbi on a large scale, building on the experiments with lending to foreign authorities that have been undertaken in recent years by the China Development Bank (CDB).\footnote{At the end of 2013, the CDB had outstanding foreign currency loans of US$ 250.5 billion and an offshore yuan-denominated loan balance of RMB 63 billion; see http://www.cdb.com.cn/english/Column.asp?ColumnId=86.}

The NDB also has a provision for lending in renminbi and taking equity stakes in infrastructure projects. Yet the push by the BRICS nations to maintain equal stakes in the NDB is likely to result in a multi-currency architecture, instead of just the renminbi.\footnote{Mathur, 2015.} At the same time, the NDB's diversified ownership should also make equity ownership less threatening.

(3) Promoting Acceptance of New Standards

Providing Attractive Alternatives: Structures...

One reason why the AIIB raised quite a stir among Western governments relates to the fear that the bank will, in one way or another, undermine existing development banks.\footnote{Lipscy, 2015.} Responding to such concerns, practitioners and observers both inside and outside China regularly argue that the China-led AIIB and NDB will complement, rather than compete with, existing institutions. In a region where infrastructure needs are high and excess savings tend to be invested in US treasury bonds against relatively low interest rates, any means that keep savings within the region should be welcomed. Seen from this perspective, the creation of new institutions that can fill the existing infrastructure investment gap, particularly in Asia, should be welcomed.

However, there can be little doubt that these new institutions will also create more competition between institutions. Infrastructure projects are large and complex, and procurement processes are challenging, meaning that substantial human capacity is needed to prepare such projects. The number of feasible projects is thus much more limited than the need for infrastructure seems to suggest. The new banks thereby also pose direct competition for the ADB, as many policy-makers outside and some
within the ADB point out. Existing institutions will thus adjust their standards in a way that they otherwise would not have, and the changes will often occur in areas such as government backing of bidding companies, opaque bidding processes, or lower environmental and labour standards. The existing institutions will also focus more on economic projects, at the cost of projects emphasizing the millennium development goals.

…and Standards

If the AIIB can establish itself as a properly functioning institution, it will also impact on the work and the standards of existing institutions, even if it does not undermine them. Although not necessarily intended, competition between projects will arise, probably with a negative impact on standards of governance, the environment and labour that took a long time to establish. This is also why co-financing between the development banks is desirable: to share risk – and thereby to spur investment also in second-tier projects – and to encourage the new lender to continue to learn from established standards. As already mentioned, opaque government procurement, the backing of companies by their home government, and labour and environmental standards can be placed under downward pressure.

Uncertainty about the standards of the AIIB was one reason why the United States put pressure on European countries to reject the opportunity to join the AIIB as prospective founding members. However, several European countries believed that exerting pressure on standards would be more effective from within, rather than from the outside. While economic opportunism clearly featured in the decision to join the AIIB, discussions in Brussels centred around how to have most influence on the AIIB's standards and procedures. The proof of the pudding is in the eating, and so the first projects financed by the AIIB and the NDB will show whether these new banks will uphold the existing standards.

This is not to overlook the fact that, on certain fronts, the creation of parallel institutions has been seen as a welcome impetus to push through change in the structures and procedures of existing institutions. The ADB, for example, has been criticized for being overly bureaucratic. On the other hand, the AIIB’s critics claim that the new bank will play fast and loose with conditionality and other restrictions on the behaviour of borrowers, allowing corruption to flourish. Non-governmental organizations have an important role to play here, by raising concerns and calling for transparency and
good practices. Here, the membership of European countries should make a positive
difference to getting the voices of non-governmental organizations (NGOs) heard.

While the NDB is less bound to such pressure from developed countries, other
challenges may be more significant, for the exact reason that it does not include
established economies. Key among these challenges is to prove the NDB’s
creditworthiness and its ability to create a portfolio of well-performing debts and
few occasions of default. The NDB (and the AIIB) is similar after all to the other
development banks in aspiring to raise capital for its operations on the international
capital markets. This appears to be at odds with the context against which the NDB was
created – namely, an aversion to the lending practices of the World Bank, which requires
certain conditions to be met in return for loans. After all, the consequences of lowering
the standards required for loans will eventually be felt by the NDB when it looks to the
international capital markets. The difference between the existing banks and the new
banks will therefore most likely be in sectors that are targeted by the NDB and the
AIIB – that is, in their emphasis on infrastructure.

Implications for Europe: The EU and its Member States

In hindsight, many policy-makers and observers in Brussels and European capitals
acknowledge that the AIIB episode put into full display the lack of a common strategy
among EU member states and an unwillingness by the member states to act on the
basis of a coordinated framework. In theory, the announcement by China in autumn
2013 of the founding of the AIIB provided a comfortable time-frame to the EU member
states to coordinate on a shared framework. In practice, however, EU members and EU
institutions largely did not act until the sudden announcement by Beijing in mid-March
2015 of the 31 March deadline for founding members to apply.

Beijing stepping up the pressure, induced discussion in several EU formats – including
in the COREPER and the EFC – in addition to contemplations at the national level.77
However, the belated joint effort to coordinate an EU position was effectively torpedoed
by the sudden announcement of the United Kingdom of its intention to join the AIIB.
Even if discussions had taken place in Brussels on an EU position on the AIIB – and
in particular the content of the Articles of Agreement that were negotiated between
April and June 2015 – the EU clearly missed a chance to develop a stronger voice with
combined force.

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77 The Maastricht Treaty provided for an economic and financial committee to be established at the start of
the third stage of Economic and Monetary Union (EMU), which began on 1 January 1999.
It is worrying that instead of binding forces to increase their power of influence – for example, in negotiations about good governance and (environmental) standards of the new infrastructure bank’s projects – European countries competed against one another in courting Beijing. Just as with attracting Chinese investments, European capitals tumbled over one another to woo China. The main goal of each individual country appeared to be to achieve more economic gain than their European neighbours. Fixated on the economic opportunities that the AIIB may provide their domestic private sector, the governments of European countries paid scant attention to the fact that the AIIB also serves Beijing’s geostrategic purposes, which do not always align with EU interests. Effectively, the Europeans fail to coordinate on a strategic vision of a world in which China is more influential, both at the EU member state and at the EU level.

EU Membership of the AIIB?

One way by which a European voice would be more easily coordinated would be through EU membership. This would go against common practice, however, as the EU is not a member of any of the development banks – except for the EBRD, where the European Commission (on behalf of the EU) and the EIB each hold 3 per cent of the subscribed capital. Representatives from China approached the European Commission to discuss the AIIB, even if the EU was never formally invited to join. Although Commission officials in private settings point to the benefits of EU membership, a spokesperson from the Commission stated that the EU did not want to get involved and would rather leave membership of the AIIB to the individual member states.78 For the moment, EU institutions are acting with restraint, as more than a few member states view the possibility of EU membership unfavourably, as this would dilute their own influence.

Against this background, it may be surprising that European Commission President Jean-Claude Juncker’s in-house think tank floated quite detailed thoughts about the possibility and practicalities of EU membership of the AIIB.79 With regard to the process, EIB participation may be relatively easy, as this institution ‘typically finances its participation in other institutions with ‘own resources’ after the approval of the EIB Board’. The process for membership by the European Commission (EC) tends to be lengthier and more complex, however:

\[G\]iven the post-Lisbon decision procedures, the May 2014 European Investment Fund (EIF) capital increase is probably more instructive as an example of how this could be done; there, the EC followed an accelerated co-decision procedure with the European Parliament and the Council, which took around five months. In the case of a more limited participation by the EC, an equity investment via an existing external ‘blending’ facility would be an alternative (for example the Asian Investment

79 European Political Strategy Centre, 2015, p. 4.
Facility, managed by DG DEVCO). This avenue could be pursued in a matter of weeks, if there was agreement on substance on the side of the EC. Ahead of that, the EC might wish to convene a meeting with the current EU Member States that have applied for AIIB membership to discuss and align strategies. An accession of EU institutions into the AIIB could be inked and leveraged with other EU initiatives – from the negotiation of China’s participation in the European Fund for Strategic Investment to an EU–China bilateral investment.\(^\text{80}\)

Although implicit, the ambitions and strategic vision of the Commission – pointing to the benefits of EU membership – are clear. This is also evident from the practical cooperation that is already taking place between the AIIB and the EIB. The EIB opened a permanent office in Beijing in June 2015 to foster cooperation between the two development banks. Also referring to the foreseen participation of Chinese banks in the EU-initiated Junker investment fund, the European Fund for Strategic Investments (EFSI), EIB President Werner Hoyer stated: ‘we are working very closely with China. It is an important partner for us when it comes to financing projects in China and Europe’.\(^\text{81}\)

**Transatlantic Relations**

While the China-led AIIB initiative posed – and still poses – a challenge to European and EU coordination, the responses of established powers also tell of a growing divide between the EU and its closest allies, in particular the United States. The United States and Japan opted to stay out of the AIIB, even as many European countries jumped onto the Chinese bandwagon.

At its core, the decision in European capitals to engage with China appears to be wise. China’s growing presence and influence in the world – especially in the field of global economic governance – cannot be stopped, but others can help to shape its decisions. As a prospective member, the Netherlands has ‘direct influence on the drafting of policies’, argued Dutch Finance Minister Jeroen Dijsselbloem in a Letter to Parliament in June 2015 wherein he expressed his government’s intention to join the AIIB. The comments by former US Treasury Secretary Larry Summers that ‘this past month [March 2015] may be remembered as the moment the United States lost its role as the underwriter of the global economic system’ reflects a similar perspective.\(^\text{82}\)

However, European capitals and companies alike should not inadvertently help to lay the grounds for a world in which Chinese or AIIB finance will be preferred in emerging

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80 European Political Strategy Centre, 2015, p. 4.
markets.83 This is especially the case because little is known about the extent to which the new bank will subscribe to the economic prescriptions and economic and social standards that are upheld by other multilateral development banks. If European non-governmental organizations and parliaments were worried about standards (not being) upheld by the ADB before – as illustrated by a Parliamentary debate in the Netherlands in February 2014 – current Chinese practices warrant even more scrutiny of the AIIB’s future projects.

This explains the rather harsh criticism by the Obama administration of its closest European ally, the United Kingdom, and its ‘constant accommodation of China’.84 In doing so, indirect reference was made to the publicly restrained stance of the United Kingdom in criticizing China over its handling of Hong Kong’s pro-democracy protests, as well as to the public statement by UK Prime Minister David Cameron that he has no plans to meet the Dalai Lama. Although European countries are still far from the generally confrontational stance taken by the United States towards China, voices are also becoming stronger in Europe that the EU and its member states should be less naïve in their relationship with China. Specifically, they are urged to ‘keep a close eye on wider geopolitical and geostrategic trends, which suggest that China may use its economic and financial prowess to pursue its unilateral political and security interests’.85

Seen in this context, the argument for EU membership of the AIIB seems opportune. It could certainly add clout also to a discussion with traditional EU allies – the United States and Japan – about their own possible participation in the AIIB.86 European countries should recognize the benefits of potential Japanese participation in the bank as a regional member, which would dilute China’s stronghold, albeit less so now than before the Articles of Agreement were signed in June 2015. While the Japanese have more economic interest in joining the AIIB than their alliance partner, they remain on a strategic par with the United States – displaying a great sense of strategic ambivalence towards Beijing, which is increasingly challenging Japanese interests in the region, including in the security field.

The general approach by European countries to engage with Chinese initiatives, which is founded primarily on economic considerations, should be scrutinized against Europe’s relationships with other countries in the region, as well as against its own long-term political, strategic and normative interests. This goes for China’s activism towards the establishment of new institutions as well as of new networks. The discussion now turns to the latter.

83 European Political Strategy Centre, 2015, p. 5.
84 Dyer and Parker, 2015.
85 European Political Strategy Centre, 2015, p. 5.
86 European Political Strategy Centre, 2015, p. 4.
Creating New Networks

Global economic governance in general is not just shaped by institutions, but also by cooperative networks. In recent years, the Chinese government has been particularly active in promoting such fluid organs and initiatives. Prime examples of this are the Silk Road Economic Belt and Maritime Silk Road; the China–Central and Eastern Europe platform (CCEE, or ‘16+1’); and regional trade initiatives. From the Chinese perspective, the latter concerns an emphasis on the APEC-led Free Trade Area of the Asia-Pacific (FTAAP) and the intra-Asian Regional and Comprehensive Economic Partnership (RCEP). Stretching across the wide Eurasian and Asia–Pacific region, each of these initiatives involves Europe directly or indirectly.

There are clear development opportunities as a result of China’s activism towards creating new networks of global economic governance, including procurement contracts and new market opportunities arising from the creation of a more favourable investment climate. At the same time, Beijing’s activism challenges European interests, in that it involves attempts by the Chinese government to (re)shape specific rules and standards to its own advantage, by emphasizing certain connections and specific approaches over others.

Looking to the future, both informal cooperative networks and more formal economic agreements are of increasing significance for tackling at least three roles: governing efficient global value chains; meeting the challenges of returning economic growth to its long-term potential; and addressing climate change. Yet while the establishment of a secure and predictable environment for trade and investment gains in importance as Asian economies have become significant outward investors, the patchwork of competitive initiatives is only deepening.

How can Europe reap the economic and political benefits of participation in these networks, without this happening at the expense of investments in global public goods and in a rules-based level playing field? How do Chinese initiatives to create new networks in the field of global economic governance impact on European interests and Europe’s ability to promote its interests in the international system? This section

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87 Dobson, 2015.
88 A rules-based level playing field – as opposed to an outcome-based level playing field – means that all firms in a market are treated the same in equal circumstances with regard to legislation, taxes and subsidies, etc.; see http://www.cpb.nl/en/publication/equal-rules-or-equal-opportunities-demystifying-level-playing-field.
addresses these questions by discussing how China’s activism in this field contributes to the three aforementioned main goals that Beijing seeks to promote. The analysis will focus on the Silk Road initiative, the ‘16+1’ framework and on competitive multilateralism in Asia with regard to negotiations on trade and investment agreements.

**Trade, Infrastructure and Europe–Asia Relations**

First announced by Chinese President Xi Jinping at Kazakhstan’s Nazarbaev University in 2013, the vision of the New Silk Road has since become a cornerstone of China’s foreign policy and public diplomacy. The New Silk Road is aimed at enhancing trade, connectivity, regional cooperation, financial integration and cultural understanding.

The idea comprises two logistical corridors: one over land, labelled the Silk Road Economic Belt; and another by sea, the 21st Century Maritime Silk Road – also known as ‘One Belt, One Road’ (OBOR). The maritime road appears to be the more important of the two, as sea routes are currently bottlenecked. The distinction between OBOR and other China-led infrastructural projects appears fluid, however, with the economic corridor from China’s north-western region to Pakistan apparently being an extension of the Silk Road initiative – and a crucial one as such, as it leads directly to the Indian Ocean and would allow China to bypass the Strait of Malacca.

The initiative is to create a network that involves more than 60 countries in Asia, Europe and the Middle East. It has already resulted in numerous specific initiatives with countries along the Silk Road routes as diverse as Pakistan and Hungary, and Singapore and Syria. In support of its Silk Road plans, the Chinese government established a US$ 40 billion Silk Road Fund in December 2014 and injected new capital amounting to US$ 62 billion into state-owned policy banks.

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89 Pavlicevic, 2015.
90 Interview with an EEAS official, July 2015.
91 For more on ‘policy banks’, see [http://www.ft.com/cms/s/0/0e73c028-e754-11e4-8e3f-00144feab7de.html](http://www.ft.com/cms/s/0/0e73c028-e754-11e4-8e3f-00144feab7de.html).
China’s recent foreign policy focus on the Silk Road initiatives is evidenced not only by the vast amount of official communication about the initiative, but also from recent actions. Notwithstanding the many references to the Silk Road by officials in speeches and statements, only one formal document elucidates the initiative in more detail. This is *The Vision and Actions on Jointly Building the Silk Road Economic Belt and the 21st Century Maritime Silk Road*, which was published by China’s National Development and Reform Commission on 28 March 2015. While this so-called ‘Vision and Actions document’ gives no specifics on projects or countries where the Silk Roads run through, it outlines the initiative’s framework, cooperation priorities and cooperation mechanisms. The personal attendance of President Xi and other high-level officials to the signing of agreements or the inauguration of projects under the Silk Road flag shows the importance of this project for China’s ambitions. Examples in this regard are Xi’s attendance in September 2014 at the inauguration of the Chinese-financed port in

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Colombo, Sri Lanka, which the Chinese see as an important stop along the Maritime Silk Road that can also act as China’s entry point to the Indian market.

Even before the Silk Road initiative really started to take off in 2015 – when the first European countries signed on, with Hungary in the lead – Beijing had already started to make its ambitions heard in Europe. This is illustrated most clearly by its efforts to shape a ‘16+1’ cooperation framework with Central and Eastern European countries (also known as the CCEE framework), which was launched in Warsaw in 2012. In December 2014, during an official visit to Europe, Li Keqiang announced the creation of an investment fund worth US$ 3 billion\(^93\) to ease access to funding for projects in Central and Eastern Europe (CEE), including those related to infrastructure and energy. The Chinese state news agency Xinhua presented Chinese investors as ‘a blessing for CEE countries, which were alerted by the 2008 economic crisis to their over-reliance on Western Europe’. The 16+1 framework was thus to be seen as an ‘engine for CEE countries to revitalize their sluggish economy and achieve recovery’.

China’s emphasis on the Silk Road network may also be seen, at least in part, as responding to other initiatives of competitive network multilateralism in the Asian region. Beijing’s primary concern in this regard is the economic element of the United States’ pivot towards Asia – that is, the negotiations on the Trans-Pacific Partnership. While the Silk Road may be seen as an informal answer to this, China’s backing of other regional trade agreements is the more direct response.

Different from China’s activities to strengthen trade and investment through informal networks stretching across the Eurasian region, its network activism on the more formal trade liberalization front focuses on the Asia-Pacific region. Here, the Chinese government’s project of choice is the FTAAP. As illustrated in Figure 8, the FTAAP builds on the recently concluded US-backed Trans-Pacific Partnership (TPP, spanning twelve countries), the China-backed RCEP (involving sixteen negotiating partners in East Asia), the China–Japan–South Korea trilateral (CJK), and the ASEAN Economic Community (AEC, negotiated among the ten members of the Association of South-East Asian Nations (ASEAN)). As elaborated below, Beijing’s emphasis on the all-encompassing FTAAP appears to be largely a symbolic strategic move.

European countries are notably absent from any of the mega trade deals that are negotiated in the Asia-Pacific region. Even so, the outcomes of these talks will obviously impact on European interests, including through their standard-setting potential. The EU

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\(^{93}\) At the same time, Li launched the second stage of the China–CEE Equity Investment Fund with Beijing’s input of US$1 billion and pledged better usage of the US$ 10 billion credit line; see Pavic, 2015; and Szczudlik-Tatar, 2014.

\(^{94}\) Ekman, 2015, p. 4.
is making its voice heard through trade talks with the United States for a Transatlantic Trade and Investment Partnership (TTIP), and bilaterally with several Asian countries. Negotiations are ongoing with China on a comprehensive EU–China Investment Agreement (IA), and on a FTA with Japan and with several ASEAN countries.

Brussels’ most recent trade strategy, published in October 2015, sets out to deepen and broaden the EU’s strategic engagement with Asia and the Pacific region, including through the launch of new negotiations with the Philippines, Indonesia, Australia, New Zealand and even Hong Kong and Taiwan. The stated ambition to strengthen relations with partners that share Europe’s values and views on many issues is a welcome sign that a more strategic perspective is being developed to the EU’s engagement with the Asia-Pacific region.

**Figure 8** Regional Trade Agreements in East Asia and the Asia–Pacific: Ongoing Initiatives

* [*] Formally expressed interest in joining the TPP.
** [**] Possibly interested in joining the TPP.

N.B. Myanmar, Cambodia and Laos (in italics) are not members of APEC and would thus not be included in an FTAAP.

Source: Adapted from Okano-Heijmans, 2014, p. 27.

The following paragraphs discuss in greater detail China’s goals in creating new networks of trade and cooperation in the Eurasian region, followed by analysis of how these relate to European interests.

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95 European Commission, 2015.
(1) Strengthening Influence in Economic Governance

Beijing’s initiatives to create and strengthen new networks contribute to the building and furthering of friendships and partnerships. Even if they do not directly strengthen China’s influence in institutions of global economic governance (and beyond), these friendships are obviously of value in such institutions. Closer relationships of interdependence – in which China commonly has the upper hand because of its vast economic clout – give Beijing improved access to information and increase the chances of countries voting with China at moments when coalitions are needed.

Considering the breadth and depth of the Silk Road initiative, a regional approach is logistically convenient for the Chinese government. This inclination to cooperate with big counterparts is one reason why Beijing is keen on cooperation with CEE as a region. In addition, there is the view in China that relations with former communist states are in some ways easier and less political than with the EU as a whole. It is thus no coincidence that the ‘16+1’ was a Chinese idea at the outset. Indeed, while the CEE countries perceived the first summit in 2012 in Warsaw as an ad-hoc high-level meeting, the Chinese Ministry of Foreign Affairs unilaterally published an action plan from Premier Wen Jiabao’s speech. This document, titled ‘China’s Twelve Measures for Promoting Friendly Cooperation with Central and Eastern European Countries’, formed the basis of a deepening of mutual relations on both the economic and political fronts.

In an attempt to foster a more balanced approach, the two sides signed subsequent agreements at the 2013 and 2014 summits. These list a series of concrete, joint initiatives largely involving trade and investment fairs and the establishment of joint cooperation mechanisms, including for the promotion of tourism and investment, and cooperation in the fields of agriculture and higher education. These guidelines grew longer and ‘wider’ over the years.

The Chinese government modified its approach not just because of unease on the part of CEE countries, but also in response to concerns shown by Brussels about ‘16+1’ cooperation. EU officials were not consulted about the Warsaw meeting and worried that the new framework could undermine EU cohesiveness, mainly with regard to EU–China policy. Responding to their concerns, EU officials have been invited to summits ever since. Furthermore, the Chinese side adjusted its rhetoric to engage and appease the EU. At the time of the third summit, for example, Chinese Premier Li Keqiang argued that China–CEE cooperation would in fact facilitate European integration, also expressing hope that ‘17 countries align our respective mid- and long-term development goals

96 Szczudlik-Tatar, 2014.
and the China–EU 2020 Strategic Agenda for Cooperation’.

Li reinforced this message several times during his visit to Serbia in December 2014 and also stated that China is committed to ensuring that future infrastructure projects would be in line with EU laws and standards.

Clearly, Brussels’ political leverage over the CEE region and its policy response towards China’s involvement in the region greatly affect the future trajectory of China’s relations with CEE. Even so, China’s activism in the CEE region continues, as illustrated by its – unilateral – move to establish a ‘16+1’ Secretariat within its Ministry of Foreign Affairs. The Chinese government appears to be adjusting its tactics, by de-emphasizing the ‘16+1’ framework and by waving the Silk Road flag. This illustrates Chinese pragmatism, as both networks share the objective of developing trade and infrastructure in the region. Beijing seems determined to stay on its course, however, as shown by the fact that Hungary became the first country to sign up to the Silk Road project in June 2015.

On the trade liberalization front, Beijing has more difficulty in getting its way with Europe. Formal negotiations between the EU and China on a comprehensive investment agreement that started in 2014 serve as a good illustration of the benefits of coordinated European action. A collective effort allows the EU to pull China closer to its position in areas such as market access, transparency, liberalization of investments and a level playing field for companies.

In the Asian context, the Chinese government, as the host of the November 2014 APEC Summit, successfully pushed for the approval of a roadmap to realize the FTAAP. China’s endorsement of the FTAAP – under discussion since 2006 – as it hosted the economic organization’s leaders in Beijing can be seen as a geostrategic statement. Clearly, the integration of these regional free-trade networks – if and when they are established – into one all-encompassing framework is a laudable aim, with an eye on untangling the

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99 In an article for the Serbian National News Agency on 14 December 2014, Premier Li said: ‘China supports the European integration process, as well as a united, stable and prosperous Europe that plays a greater role in the international community. […] China’s cooperation with the sixteen CEE countries will not result in fragmenting the European Union. Much to the contrary, it will help deepen cooperation between China and the European Union and narrow the development gap between the eastern and western parts of the European Union. […] China–CEE cooperation is undoubtedly part and parcel of China–Europe cooperation, and the two could naturally go in parallel and be mutually reinforcing’, *Tanjug* (Serbia’s state news agency), quoted in Pavlicevic, 2015.


101 Pavlicevic, 2015.

102 Zha, 2015, p. 9
noodle bowl of highly divergent regional FTAs that cover different sectors and involve diverging rules.

The vast challenges that come with the creation of the FTAAP, while other talks are still ongoing, suggest that Beijing’s firm advocacy of this partnership was largely of symbolic value. Indirectly, Beijing’s move appeared to counter the United States’ push toward the TPP – agreement on which was finally reached in October 2015. In this sense, China’s promotion of the FTAAP was also a defensive move, showing that the Chinese government is ready to take the initiative even though it is obvious that actual realization of the comprehensive FTAAP agreement is beyond reach any time soon. It portrayed Beijing as a government that believes that it is better to pursue something unobtainable than to watch from the sidelines, as it was excluded from TPP negotiations.

**Contributing to Regional Economic Integration**

Notably, the aforementioned ‘Vision and Actions document’ that elucidates the Silk Road initiative includes more than 100 references to the word ‘cooperation’, while also emphasizing that all countries are welcome to join the initiative. It is explicitly stated that the initiative is aimed at ‘jointly creating an open, inclusive and balanced regional economic cooperation architecture that benefits all’.

This clearly shows the ambitions of the Chinese government and its vision to promote bottom-up regional cooperation. While such informal cooperation creates new economic opportunities for the governments and companies involved, China generally has the upper hand, as its vast market and outward investment potential are irresistible to individual countries and businesses. In addition, the cumulative results of its efforts commonly go unnoticed, allowing China to hide its size.

Also in the ‘16+1’ framework and trade liberalization efforts, the contribution of these networks to fostering regional economic cooperation is emphasized. In these formats, however, the competitive elements are more evident. While China–CEE cooperation is also seen as a challenge to EU integration – at least from the perspective of Brussels and several member states – China’s firm endorsement of the FTAAP proposal added to the already existing tensions in the Asia–Pacific region between China on the one hand, promoting intra-regional Asia-only cooperative networks, and the United States and Japan on the other, aiming to further intra-regional networks in the Asia–Pacific.

Keeping Foreign Reserves in the Region

Capital investments by the Chinese government to bridge the infrastructure deficit in the Eurasian region are welcome, and not just because they contribute to economic dynamism. To the Chinese government, such investments also serve to keep reserves in the region and to diversify and invest the US$ 4 trillion in foreign exchange reserves that it holds. In this sense, investments in the Silk Road Fund, domestic policy banks and the China–CEE fund thus resemble capital injections in the AIIB and NDB.

Like many governments in the Asian region, China has long spent its excess savings in US Treasury bonds against relatively low interest. Beijing is now shifting its focus to increasing China’s investment in neighbouring nations and in countries along the Silk Road routes, including in Europe. This serves the Chinese government in at least three ways. First, it largely keeps savings within the region and contributes to China’s politico-strategic goals of building friendships and partnerships with neighbouring countries. At the same time, it puts a brake on China’s indirect support of the United States by strengthening Washington’s spending power and adding to the position of the US dollar as the world’s reserve currency. Finally, as elaborated below, the diversification of capital investments into a variety of funds and diversity of regions also serves China’s domestic goal of spreading risk, by having more than one kind of investment and thus more than one kind of risk.

(2) Furthering Domestic Goals

Rebalancing the Economy

Beijing’s Silk Road initiatives aim above all to rebalance China’s economy. Since 2014, President Xi Jinping and other high-level officials started floating the idea of China’s ‘new normal’. This newness is said to lie in lower economic growth rates, diversification of the economy, and a shift away from input and investment towards innovation as the main driver of the economy. This should also contribute to a more equal distribution of benefits across regions. Shifting towards a more sustainable level of growth of around 7 per cent may be only natural after years of double-digit growth. The other two elements – economic diversification and a shift towards innovation – are more challenging, however, as they require structural reforms and long-term policies.

The New Silk Road and, to a lesser extent, the ’16+1’ framework contribute to these objectives by facilitating the foreign expansion of certain sectors. OBOR does so particularly to regions that connect China’s western provinces to neighbouring countries and to sea routes. China’s excess domestic supplies are thus channelled into overseas markets, in part by stimulating foreign demand for those industrial exports, including cement, steel and aluminium – three of the biggest industries facing over-capacity
issues right now in China. This reorganization of the supply chains linking China to the rest of the world will allow for the relocation of labour-intensive production to other countries, while a growing proportion of their output is likely to be sold in China, as a way of furthering domestic consumption.104 Again, OBOR and the China–CEE network address the main constraints to this reconfiguring of international commerce by improving transport and communications links.

Free-trade and other economic agreements contribute to this same goal of reconfiguring international economic relations by reducing barriers to trade, including customs duties and non-tariff barriers. At the same time, excluding countries from such negotiations or the postponing the opening of negotiations can signal disagreement with economic policies. This partly explains why economic talks between the EU and China are currently limited to the fields of investment, procurement and intellectual property rights, even if trade is the more substantial issue between the two sides.

As the European Commission points out, there is inherent tension between China’s state capitalism and Europe’s desire to promote openness and respect of international trade rules.105 Seen in this context, Europe’s postponement of the opening of talks on a comprehensive trade deal resembles the promotion by Washington of the Trans-Pacific Partnership – even if the first is a bilateral undertaking and the latter a regional one. On both fronts, and in these more formal settings, the EU and the United States are better able to lure China out of its comfort zone.

Policy on Bank Reform

In mid-April 2015, the State Council (China’s cabinet) promulgated reform plans at three state-owned non-commercial big policy banks: the China Development Bank (CDB); the Export–Import Bank of China (EIBC); and the Agricultural Development Bank of China (ADBC). Renewed emphasis was given to the role of these banks in supporting government policies and strategic goals. This includes financing infrastructure and other policy priorities within China and abroad, as well as addressing China’s slowing economic growth and the rising bad debts of its commercial-banking sector. The government is thus also looking to these banks to reinforce support for its ‘One Belt, One Road’ strategy.106

More specifically, the CDB is to focus on ‘stabilizing growth and structural adjustment’ and to increase support to strategic areas and sectors in difficulties. For its part, the

104 Elek, 2015.
106 The other two – domestic – engines of growth identified by the National Development and Reform Commission in this context are the Beijing–Tianjin–Hebei region and the Yangtze River economic belt.
EIBC will support the government’s ‘going-out’ strategy and is to ‘persist in its role as a developmental financial institution’, while the ADBC should separate policy-oriented lending from its other businesses. According to most observers, this reverses the trend of recent years in the CDB and EIBC, which had moved beyond their original goals ‘to carry out Beijing’s economic orders’ to aggressively pursue commercially oriented deals.\textsuperscript{107}

The reform plans also involved recapitalization of the policy banks. While the Central Bank was to inject US$ 32 billion in reserves into the CDB and an additional US$ 30 billion into the EIBC, China’s Ministry of Finance is to recapitalize the ADBC with an unspecified amount.\textsuperscript{108} This is yet another indication that China’s leaders are prepared to mobilize China’s considerable financial resources to put the scheme into action and to extend Chinese sway across Asia.

\textbf{(3) Promoting Acceptance of New Standards}

\textbf{Trade Liberalization Light}

China’s regional trade deals of choice – the RCEP and the FTAAP – portray a much lower level of ambition for trade liberalization than the TPP or any agreement that the EU is negotiating. This may partly be explained by China’s level of development, as well as by its distinct political–economic system, and its greater tendency to pursue geostrategic goals through trade deals. Trade deals thus aim not just to add economic value, but also to consolidate partnerships that benefit China by fostering stability and expanding China’s influence through greater economic interdependence.

Beijing has been steadily investing in and diversifying its trade policy in recent years, as is apparent from active negotiations with South Korea and Australia, as well as with more partners in the China–Japan–South Korea trilateral and the RCEP. While the Chinese government is contemplating participation in the TPP, it will not risk being rejected if it does so, and is therefore unlikely to ask until it can be sure that the US Congress will accept it. In relation to this, Beijing is also restrained because the TPP would require more domestic reforms than China is comfortable with at this point, including the opening of markets in services and investment, and agreeing to rules in sensitive areas such as the role of SOEs and internet access.

\textsuperscript{107} See, for example, Wei, 2015. It should be noted that while most agree that the reforms seem to be a step away from market-oriented reform, contrasting views are also heard.

\textsuperscript{108} Wildau, 2015.
The standards negotiated in the TPP and the TTIP will have global effects, however, as they will set the tone for future deals. Their early conclusion is therefore of value also in the relationship with China. The final aim should be, however, to agree on new common standards – in particular between the EU, the United States and Japan. Failing to do so would contribute to the patchwork of regional and bilateral agreements, resulting not only in the famous rules-of-origin noodle bowl, but also in a noodle bowl of varying rules and regulations in different places.

For its part, EU-China investment negotiations are very much about market access – that is, about investment liberalization. The existing bilateral investment deals that most EU member states have with China are about investment protection, and the new agreement should clearly deliver more. The standard-setting value of this first stand-alone investment treaty for the EU obviously adds to its importance. China is thus challenged to show a significant level of ambition, also because only then will the EU positively answer its calls for the negotiation of a wider trade agreement. Notably, China has also started to use the terms that the EU has been employing with regard to the agreement – namely, ambitious and comprehensive.109

**Government Procurement**

China’s Silk Road initiative allows the government to guide the economy by emphasizing certain sectors – that is, by deciding to develop infrastructure, including roads, ports and energy grids in particular. This may be labelled indirect government support, as the Chinese government decides which sectors of the economy are advantaged in their activities abroad. It is thus no coincidence that projects under the Silk Road flag benefit the sectors where China faces most over-capacity domestically. While many governments throughout the world have such industrial policies in place, the financial backing of this activism in China makes it unique in comparison to others.

More direct government support is discernible when Chinese companies are given significant advantages in winning contracts for specific projects abroad. Even if it is not formally assured that Chinese companies will win the contracts, there should be little doubt that Chinese companies are the biggest beneficiaries. One reason is that they know of projects at a very early stage, and because of the close links between Chinese officials and businesses.

This is already happening. Similar to China’s economic cooperation – that is, Chinese or Asian-style development assistance – Chinese companies are generally contracted for Silk Road projects. This includes the building of ports in Sri Lanka, Bangladesh and Pakistan. From other countries’ perspectives, this may create unfair competition

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109 Interview with an official of the EEAS, 14 July 2015.
considering the importance of these projects to the Chinese central government and the amount of state backing that China is prepared to do for a Chinese company to win procurements.

This issue also relates back to China’s status in the WTO. There are clear rules for government procurement, but foreign companies have complained for years that Beijing boosts domestic companies and gives them an unfair advantage in its procurement market. China’s regulatory framework governing such economic activity is said to be opaque, fragmented, inconsistent and unevenly implemented. It will be important for the EU to stand firm when it comes to investments in the EU, fair bidding processes and government backing of bidding companies, otherwise the Silk Road will be far from a ‘win–win’ for Europe and China.

**Implications for Europe: The EU and its Member States**

China’s attempts with the Silk Road project and the ‘16+1’ cooperation are clear signs that it wants to link its domestic market through Central Asia to the European market. The EU, with more than 500 million inhabitants, the combined largest market in the world and companies with lucrative technologies, has a strong bargaining position in this regard. At least in theory, this gives the EU and its member states leverage to ensure that China’s investments in linking these markets proceed under conditions that are sure to benefit Europe as well. Proposed agreements and projects should be regarded with particular scrutiny until European companies’ access to the Chinese market is on a par with Chinese access to the EU market.

**Whither the ‘16+1’ Framework?**

The fact that China has masterminded a network that includes eleven EU member states as well as five other European countries resulted in considerable unease in Brussels and in several EU member states.\(^\text{110}\) The EU dismisses China’s suggestion of regarding the framework as an integral part of EU–China relations.

Such apprehension of the framework may seem hypocritical when set against the common practice of every EU member state to engage with China bilaterally in addition to the joint EU–China channel. Yet the ‘16+1’ framework is perceived differently, mainly for three reasons: it concerns a regional grouping rather than a bilateral relationship; it involves EU and non-EU countries; and it mainly concerns a competence that is shared by the EU and its member states – namely, transport.\(^\text{111}\) In addition, it has been

\(^{110}\) Interviews with various EU officials, May–July 2015.

\(^{111}\) Interviews with various EU officials, May–July 2015.
suggested that some of the CEE countries that are also EU members appear to feel closer to Beijing than to Brussels, as they feel 'second rank' in the EU.\textsuperscript{112}

For their part, CEE countries are balancing a sense of unease arising from China's activism and at times unilateral steps, with the economic and strategic benefits of working with Beijing. The ‘16+1’ framework gives them unique and regular access to senior Chinese officials as well as to Chinese funds. Not all of the sixteen CEE countries benefit equally from China's economic proposals, however. Balkan countries, for example, 'are keen on China's infrastructural projects, and the credit line is being used mainly in this region', while the EU member states are mostly interested in attracting foreign direct investments (FDI).\textsuperscript{113}

Chinese attempts to convince the EU that cooperation will be conducted in accordance also with EU law, and that ‘16+1’ does not undermine the EU's China policy and the EU's cohesiveness, have served to alleviate some of Brussels' concerns. Even so, the complicated matrix of cooperation among China, CEE countries – including EU member states and other European countries – and the EU indicates that it will remain a challenging format in the future.

**Europe: Retaking the Initiative**

An important outcome of the June 2015 EU–China Summit high-level meeting was the launch of the Connectivity Platform. Importantly, this platform aims to improve infrastructure and transport links and to develop synergies between existing European and Chinese projects, including the Trans-European Networks, the South European Network Organizations and, of course, the Silk Road. European investment in this region halted in recent years and the Chinese are jumping into the gap. In addition, the Connectivity Platform attempts to broaden its scope from transport or infrastructure alone, to include also, for example, energy, information and communications technology (ICT) projects and people-to-people exchanges.

In furthering this initiative, Brussels showed itself capable of reshaping Asian ideas into joint strategy and action. Both the Asian buzzword of late – Connectivity – and China's flagship initiative – the Silk Road-inspired ‘One Belt, One Road’ – are transformed into an EU–China initiative that conforms with European economic and strategic interests. As such, it constitutes an attempt to avoid a situation where China defines the issues, and instead to explicate what the EU wants and what standards the EU wants to

\textsuperscript{112} Interview with a representative of the Dutch Ministry of Foreign Affairs, March 2015.  
\textsuperscript{113} Szczudlik-Tatar, 2014, p. 2.
Importantly, the Connectivity Platform also allows the EU to diffuse tensions between EU member states by diminishing the importance of the ‘16+1’ framework.

The EU, by taking action before member states do so individually, moderates the internal competition for China’s favour. Furthermore, the Connectivity Platform is a way for the EU to continue to export its standards in the face of massive China-led infrastructure spending. Although EU member states are already legally held to certain standards, the Connectivity Platform can be used to export these to the EU neighbourhood and beyond.

While Chinese banks are making their way into Europe through Chinese funds and Beijing-backed initiatives, they also enter at the specific invitation of Europe. They are also likely to be involved in the European Fund for Strategic Investments (EFSI), more commonly known as the Juncker Plan. Launched in 2014 as the flagship project of Jean-Claude Juncker – the President of the EU’s executive arm – this plan aims to create an investment friendly environment and to mobilize investments of at least €315 billion in three years in Europe’s real economy.

Chinese interest in this plan is welcomed, as Europe seeks to attract greater Chinese investment in Europe. From China’s perspective, the initiative neatly fits its own economic and geopolitical agenda. Reportedly, Chinese banks are ready to invest billions ‘if the right conditions are met’.

Notwithstanding the launch of the Connectivity Platform and strengthened European coordination, cracks have already begun to appear in the EU’s aspiration not to repeat its faulty, lagging response to the AIIB initiative and instead to develop a more coordinated approach to EU–China relations. Hungary has already signed an agreement under the Silk Road flag, and France recently signalled its intention to be next.

The following, final chapter of this report will gauge Europe’s response to the diversity of Chinese activities in the field of global economic governance and assess how the EU and its member states may best defend their interests in the future.

Also on the trade front, Europe appears to be increasingly acting with a comprehensive view. The years of emphasis on ‘WTO only’ have passed and the EU is actively pursuing regional and bilateral trade agreements. Speaking on the future of EU trade policy in May 2015, EU Trade Commissioner Cecilia Malmström emphasized its importance to furthering two goals: building prosperity; and protecting and projecting European values.

114 Interview with an EEAS official, July 2015.
117 Malmström, 2015.
is evident both from the vast number of negotiators involved and from discussion in the European Parliament and society more generally – relations with Asian countries are clearly second. The two regions are obviously linked, as illustrated by the – sometimes rivalling – standard-setting ambitions of agreements under negotiation. Looking to the future, this connection needs be more formalized – especially for the EU, United States and Japan – in order to prevent a ‘regulation noodle bowl’ and instead to strengthen coherence. At the same time, talks with Beijing are a crucial way to ensure that an open stance is maintained with Europe’s biggest trading partner in Asia, despite the obvious differences in political–economic systems.

**Europe–Asia Relations**

Despite the degree of unease in Europe over China’s perusal of the ‘16+1’ framework, both Brussels and individual European capitals are by and large very welcoming of Chinese initiatives to create new economic networks. This open stance may be only natural, since China is one of Europe’s ten strategic partners with which it aims to further deepen bilateral ties. But how do other European strategic partners with a significant stake in the region perceive China’s activism? A brief overview of responses from India, Japan, the United States, South Korea and Russia shows that they are not equally, or at least not so indiscriminately, welcoming of China’s plans.

Perhaps unsurprisingly considering the long-standing rivalry between India and China, many Indian security analysts see the Maritime Silk Road as an effort to encircle the subcontinent. Worries exist about how the Maritime Silk Road will be implemented and whether its geo-economic rationale or security objectives will dominate. Like other countries, India was invited to be part of the Maritime Silk Road, but its response has been lukewarm.

Together with the United States, Japan is most vocal in voicing concerns about China’s increasing assertiveness in the South China Sea, while it is also in dispute with Beijing over sovereignty of the Diaoyu/Senkaku Islands. China’s increased activism in land reclamation and project building in disputed territories, and its intrusion of other countries’ economic zones, clearly add fuel to the fire. Chinese efforts to control larger parts of the maritime sea-lanes that connect Asia with Europe are therefore met with significant opposition in Tokyo and Washington. In various forums, Japanese officials are calling for greater efforts to protect the rule of law and freedom of navigation. Open conflict in the South China Sea, however, would harm China’s plans for the Maritime Silk Road. While it is thus unlikely that Beijing would consciously initiate

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118 Europe’s four other strategic partners – Brazil, Canada, Mexico and South Africa – as they are not a direct party to China’s network activities, spanning the Eurasian and the Asia–Pacific region.

a direct conflict, the rising tensions make for a dangerous situation that impacts on any country or company with economic interests in the region.

By comparison, South Korea is very restrained in criticizing its big neighbour. While this may be only natural considering its much smaller size, the fact that it is not openly siding with Japan and the United States is indicative of the more neutral stance that South Korea takes to rising Chinese influence in the region. Like Europe, South Korean representatives have a more pragmatic take on the issue, as illustrated by the comment of one official that ‘South Korea’s application as a founding member of the ADB was stimulated by its desire not to be treated unfavourably by China’.\textsuperscript{120} It deserves mentioning that the same is probably true for Australia.

Despite the warm rhetoric and string of agreements in Russia–China relations of recent years, many Russians worry about China dominating their bilateral relationship.\textsuperscript{121} This explains why Russia has not unilaterally been forthcoming in supporting China’s OBOR initiative, which constitutes, from Russia’s perspective, an open road to Europe. This is illustrated most clearly by Russian resistance to the creation of an SCO Development Bank. However, the agreement between China’s President Xi Jinping and Russian President Vladimir Putin in May 2015 on harmonizing the development of the Russian-dominated Eurasian Economic Union (EEU) and China’s Silk Road Economic Belt showed that Beijing increasingly has the upper hand. Sanctions by Western countries on Russia certainly give it a stronger incentive to develop its economic ties with China.

Although this concise overview admittedly only touches on the surface of other strategic partners’ perceptions of Europe, it clearly shows how each of these countries is directly affected by, and is not singularly forthcoming to, China’s initiatives. This should have the EU and its member states thinking about their own response, as well as about how their choices affect those of the other strategic partners with a stake in the region. The concluding chapter of this Clingendael Report discusses this in greater detail.

\textsuperscript{120} Interview with officials of South Korea’s Ministry of Foreign Affairs, The Hague, July 2015.

\textsuperscript{121} See, for example, Bond, 2015.
In 2015, Chinese leaders put on full display their ambition and determination for the China government to become an agenda-setter in global economic governance in Asia and, to a lesser extent, also in parts of Europe. Barring an unforeseen crisis, Beijing’s posture will be further developed, meaning that European capitals will increasingly face the choice of engaging, co-opting, or confronting China.

This should urge European countries to consider their responses. Europe can gain quite a bit from a China that is more integrated in the system of global economic governance and from the positive effects of China’s activism on the investment climate in the Eurasian and Middle Eastern regions. At the same time, however, European nations need to make sure that Chinese undertakings do not result in a ‘low-cost international order’ that benefits China at the expense of European interests, as some suggest.

Ultimately, China’s growing investments in Europe will also provide it with increasing influence, which may divide the EU on an increasing number of occasions. This in turn will increase the likelihood of individual European member states opposing action by Brussels, for example if it tries to introduce anti-dumping regulations against China. Lack of a clear-cut common vision by European countries – including a set of long-term priorities and positions – could become a weakness when dealing with a strong partner that already has one.122

European Representation and Coordination

Previous chapters have shown that China is making some progress in strengthening its voice in existing institutions and in raising support for altering labour and environmental standards, government procurement and transparent bidding processes, debt sustainability and economic policies. Beijing is also leading initiatives to create parallel institutions, in which China’s interests are better represented. As a welcome extra, this also adds a sense of urgency to the reform of the traditional institutions. Finally, China is inviting countries in the Eurasian region and the Middle East to support the Silk Road projects, while also calling on countries in the region to participate in its own version of formal trade multilateralism.

122 See also Sieren, 2014; and Ekman, 2015, p. 4.
Resisting China’s efforts and not joining its new initiatives may result in missed opportunities for both potential funders and entrepreneurs, and eventual beneficiaries in Europe. That being said, China’s best interests do not always align with European interests. Balancing the benefits and the pitfalls proves to be challenging for any single country, let alone for the group of countries that are united in the EU. This is especially so at a time when the number and variety of European subgroupings that cooperate or compete in global economic governance are increasing. Consider, for example, strengthening cooperation between the Eurozone and non-Eurozone countries; and the CEE member states and other EU member states; as well as the European countries that are more welcoming of China versus those who tend to see its rise with caution. These complement the more traditional division between more dynamic neo-liberal countries in the north and some more protectionist countries in the south of Europe.

Discussions at the EU level are more important now than at earlier times, as these could help in collecting additional information and adopting a common approach.\textsuperscript{123} China’s activism is certainly not about to diminish and EU member states may expect in the coming years to be increasingly invited by Beijing to join other institutions or informal frameworks. Such lobbying will occur both directly with individual EU governments, as well as more indirectly from governments that are already involved in such initiatives or by local European actors who may enthusiastically support specific projects.\textsuperscript{124} This is already happening, as representatives from the business community are eager to gain a share of the pie and generally overlook the longer-term consequences that may come with it.

Many government officials in Europe admit that the faulty, lagging response to the AIIB initiative should not be repeated in the future and that a more coordinated approach to EU–China relations needs to be developed. However, serious challenges to a better approach remain. They include a lack of willingness to coordinate better at the EU level or even to share information (as evidenced by the AIIB episode); distrust among member states (as illustrated by the fact that, for several years now, the intra-EU Asia–Oceania Working Party (COASI) has been downgraded from a meeting of (vice-)directors for Asian affairs to one for policy officials\textsuperscript{125}); and the fact that, despite the depth and breadth of economic ties, strategic elements of relations with China are just not a political priority in Brussels or in European capitals. Attention is being given to more immediate issues, including the Greek financial turmoil and the immigration crisis in Europe.

\textsuperscript{123} Ekman, 2015, p. 4.
\textsuperscript{124} Ekman, 2015, p. 4.
\textsuperscript{125} Interview with a representative of the Dutch Ministry of Foreign Affairs, March 2015.
What is missing is a real China taskforce – one that would entail regular assessment of the state of relations with China among all of the European officials dealing with China. Even the annual White Papers on EU–China relations that were commonly prepared before the adoption of the Lisbon Treaty in 2009 are no longer published. This appears to be the result largely of the intra-EU bureaucratic struggle; the EEAS and European Commission have been engaged in a fight over who is responsible for what. The difficulty of the task is furthermore compounded by the vast number of actors that are involved in global economic governance issues and in EU–China relations. Figure 9 lists the main actors and their responsibilities at EU bodies in Brussels.

Figure 9  Key EU Actors Involved in Policy-making in the Field of Global Economic Governance (with a Focus on the EU–China)

Source: Authors’ compilation.

Judging from comments by various EU officials, only now is there the realization in Brussels that Europe needs a common framework on China. This is reflected in the adoption of several recent documents negotiated with China, including the ‘EU–China 2020 Strategic Agenda for Cooperation’ and the 2015 ‘EU–China Summit Joint Statement’. Clearly, however, such joint agreements are a far cry from a serious analysis of the interests of the EU and its member states. The various European capitals appear to have less certainty about the necessity of prioritizing the EU level rather than bilateral relations. Consider, for example, the quick succession of the Dutch state visit to China in 2015 following the high-level visit of Chinese President Xi Jinping to The Hague in 2014.

126 Interview with an EEAS official, July 2015.
The ineffectiveness of cordonning off the various aspects of EU–China relations should be recognized and managed. A wide-angle view of China’s actions is necessary to see the larger trends and then find the opportunities and areas of concern for Europe. Of interest in this regard is the proposal to create an ‘early warning mechanism ‘to forewarn the European Commission of upcoming developments of strategic significance’. This suggestion should be regarded as an attempt to draw lessons from the AIIB episode, when many EU actors – in Brussels and in European capitals alike – were aware, but when political action was not taken. Clearly, a more coordinated Europe-wide response could have been organized that would most likely have translated in a better bargaining position for participating European countries in the negotiations with China and other (prospective) members.

The vast ambitions of the European Commission are perhaps most explicitly stated in a piece by Jean-Claude Juncker’s recently established think tank, the European Political Strategy Centre: ‘The European Commission should lead in facilitating a loose coordination of EU Member States that are joining the AIIB, while also ensuring that European institutions are represented and an “early warning mechanism” is launched to prevent slow and uncoordinated decision-making in the future’.128

The inter-service meeting called by the EEAS about the Silk Road initiative is an example of how things should be done. This meeting brought together officials from fifteen different sections that were all involved with or affected by the Silk Road. Inter-institutional dialogue is needed to create and maintain a framework for actions with China. China’s actions with the NDB and the AIIB and how these relate not only to the Silk Road initiatives, but also the internationalization of the renminbi, show just how interconnected the Chinese actions are. An uncoordinated approach from the Europeans, as has been the case in the past, allows China to play European capitals against each other.

Towards Greater EU Representation?

Debate has increased in recent years about a possible joint representation of Eurozone countries in certain institutions of global economic governance. Such a ‘Eurogroup’ representation in the IMF may seem a far-fetched idea considering the difficulty that came with the recent reshuffling of constituencies. Nevertheless, there is reason to weigh the opportunities against the benefits now, as further downscaling of the vast voting power of European countries will remain on the agenda.

127 European Political Strategy Centre, 2015, p. 4.
Officials are divided on the benefits of common EU representation at multilateral institutions. At the IMF, for instance, pairing EU countries with others through the constituency system ensures that these EU member states are also able to represent the wishes and needs of non-EU countries. This can improve the standing of European nations among countries with less influence. Furthermore, there is the added benefit that if EU member states do not agree on certain issues, they can raise these differences during meetings instead of diluting their message beforehand to make it acceptable to all of the EU member states.

On the other hand, EU member states contradicting or challenging each other too often can undermine the EU’s standing in the eyes of the rest of the world. The Greek crisis and the threat of a potential British exit from the EU (the so-called ‘Brexit’) are already causing European unity to be questioned; additional disunity may discredit the EU further.

Set against this context, it may be unsurprising that the establishment of the AIIB is considered by some as an opportunity for Eurozone countries to put this new form of representation to the test without having to give up an established position. The June 2015 Letter to Parliament by the Dutch Minister of Finance, which floated the possibility of having one Eurozone seat in the twelve-member Board of the new bank, shows that this option is now seriously on the table. Complicating the challenge, however, is that only eleven of the nineteen Eurozone countries are AIIB members.

One important benefit of having a Eurozone seat is that this would ensure consultation among countries so that they develop a joint position. Furthermore, third countries – including China – would be less able to play European capitals off against each other.

However, a joint Eurozone seat would also do away with certain benefits that come with other forms of representation. The like-mindedness of countries may be higher in other formats; in the ADB, for example, the Netherlands is in a group with Canada and Ireland – countries with which it shares more values than with some southern European members. At the same time, this particular format complicates any effort to develop a joint European position. Mixed groups with developing countries also have certain benefits. Acting as a bridge-builder behind the scenes may have real benefits in formal and informal settings, and is thereby a way to wield soft power multilaterally. Consider, for example, the fact that the Netherlands has booked some successes on this front in the IMF, where it is in a group with Belgium and several CEE countries.\(^{129}\)

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\(^{129}\) The constituency is comprised of: Armenia, Belgium, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Georgia, Israel, Luxembourg, Macedonia, Moldova, Montenegro, the Netherlands, Romania and Ukraine.
EU–Asia Cooperation

In order for a strong and effective common framework for relations with China to work in practice, Europe must cooperate with other countries in the region. An EU–China strategy must take into account a broader EU–Asia strategy and bilateral relations in this region. The ‘One Belt, One Road’ initiative, the AIIB and the NDB, as well as the FTAAP and RCEP – among others – show the importance of regionalism for China’s activities in global economic governance. Against this background, the integration of an Asian and China strategy by the EU is necessary to protect and pursue European interests.

There are diverging interests in Asia towards the Chinese activities. Pakistan and Sri Lanka have already started negotiations or signed agreements with China for infrastructure projects linked to the Silk Road. Other countries, for instance Indonesia, are reportedly also interested in securing financing for infrastructure projects through the AIIB or the Silk Road Fund. However, there are also concerns about the increased Chinese presence among its neighbours. Some countries worry that China’s investments will not be as win–win as Beijing likes to emphasize. The use of Chinese companies for infrastructure projects does not benefit local economies as much as it does the Chinese economy. This is an area in which Europe can back up Asian countries to apply pressure on China to change its practices. Furthermore, there are also areas in which the interests of China and its neighbours conflict, such as in the South China Sea.

For this policy to be effective, European capitals must work together and present a strong united front. In this way, they can leverage the power of the single market, the strongest leverage that the EU has over China. This will allow the EU to work with and to back up countries in the regions. It will also allow European countries to increase their engagement with Taiwan and the Dalai Lama, two issues about which the Chinese government is historically sensitive. A united European front, including non-EU members at times, can prevent harsh reactions from China of the kind exemplified by the cut on imports to China of Norwegian salmon after the 2010 Nobel Peace Prize was awarded to Chinese dissident Liu Xiaobo. Meanwhile, not doing so will most certainly undermine Europe’s standing as a promoter of democratic values, civil liberties and freedom of speech.

A final consideration for the EU and its member states should be its relations with Japan. As the second biggest economy in Asia, Japan is China’s most direct competitor and the countries are often at odds. After the launch of the AIIB and the Silk Road Fund, the Japanese government pledged US$ 110 billion for ‘quality infrastructure investment’ in the region and to support the ASEAN integration efforts. Furthermore, there is the potential for competition between the Japan-led ADB and the China-led AIIB. As such, it is important for the EU and its member states to approach relations with Japan in a strategic manner, so as to serve European interests in the region best.
Transatlantic Cooperation

Whereas Europe is no serious player in the field of Asian security, the United States is at the heart of most territorial disputes. This necessitates a clear and strong China strategy on the part of the United States. As can be seen in its so-called ‘pivot’ to Asia, the reaction to China’s actions in the South China Sea, the exclusion of China from the TPP and the pressuring of allies not to join the AIIB, the United States is generally confrontational towards China. The China threat paradigm is present among most prominent US politicians. Europe has less of these confrontational issues with China and other countries in Asia. Although the US alliances in the region have long contributed to the stability that Europe needs to preserve its economic interests, the increasing importance of China to its neighbouring countries is changing the status quo. The more confrontational policy of the United States towards China and the region requires more well-thought strategies for how the EU and its member states can protect their interests. It is thus important for Europe not to be seen as the lapdog of the Americans. Europe’s defiance of US wishes about joining the AIIB can be seen as an example of the diverging interests of European capitals and Washington.130

One important aspect of current transatlantic relations in economic governance is the ongoing negotiations over the TTIP. A massive modern trade and investment deal between the world’s two largest economies (the United States and the EU single market), which are both highly developed, will have ripple effects for all other trade deals, whether they are bilateral or through the WTO. The standard-setting potential of this deal and the importance of the US and EU markets can put pressure on other countries to raise their standards too.

One aspect of the negotiations over the TTIP has become controversial, particularly in Europe. The issue of investor-state dispute settlements (ISDS) has been wildly unpopular throughout the continent, as the lengthy discussions in the European Parliament show. Public criticism over this has already caused problems in the negotiations over the TTIP and the trade and investment deal negotiated between the EU and Canada. This can have consequences on the inclusion of ISDS in the EU–China Investment Agreement. Officials of the EU Commission stress the importance of ISDS, especially in the case of a comprehensive investment agreement with China, because of the lack of transparency and independence of the legal system in China. ISDS offer European companies an avenue to protect their business interests without having to work through the Chinese legal system. This shows the importance of transatlantic relations to the EU’s relations with China and the rest of the world.

130 See also Twining, 2015.
Tensions between European and US interests do spring up from time to time, however. One example is the reports that the United States has been attempting to use the TPP to get Asian countries to go against the agreements with the EU regarding geographical indicators. The EU’s use of geographical indication for its intellectual property is controversial in America, where the general opinion is that this would hurt US businesses. Should the US continue in its attempts to undermine the EU’s position on geographical indication in Asia, this would hurt European interests in the region and in the world in general. Transatlantic cooperation is therefore important from a European perspective, because of the weight that the United States carries in the Asian region that Europe currently lacks.

The relative lack of weight that Europe carries in the Asian region other than in the trade field, however, also offers Europe interesting opportunities. In its relations with China, for instance, Europe can and has taken a much less confrontational stance. This gives the EU and its member states a certain measure of freedom in its decisions and is probably a more effective way of engaging with China than the containment strategy that is employed by the United States.

**What Lies Ahead?**

While all of the recent Chinese initiatives raise questions about the current state of affairs in global economic governance, they should also be viewed as departure points for future developments. How will the arena of global economic governance change in the years to come? Can we expect further institution-building or the demise of existing institutions? Where will China’s focus lie and how can the EU and its member states best react to this? Addressing these long-term strategic thoughts will allow European capitals and Brussels to uphold their interests and ambitions in this field.

The turmoil in the Chinese stock market in July and August 2015 has stirred up widespread debates about the direction that the Chinese economy and political system is headed. The statements and actions of Chinese officials have been rather conflicting. The devaluation of the renminbi has been justified as an attempt to give it a more realistic and market-determined price. However, this move has also been interpreted by some as a way to support China’s faltering exports. Moreover, the Chinese government’s far-reaching intervention on the stock market showed the tension in China between an increasingly market-driven economy and continued state control. The Chinese government froze short-selling and initial public offerings; used government funds to increase investment, forcing pension funds and cashing brokers to invest again; and pushed the security bureau to investigate and punish individuals for market manipulation and ‘spreading market rumours’. This plays into the larger debate about the future of China in global economic governance.
The rebalancing of the Chinese economy from exports and investment-driven to technology innovation and consumer-driven was always going to result in turbulence, but this has come quicker than many expected. The impressive (nearly) double-digit growth figures that China continued to achieve in the years following the 2008 global financial crisis had been gradually slowing to an official figure of 7 per cent – what the Chinese leadership now calls ‘the new normal’. Coupled with falling exports and real estate prices, and an inflated stock market releasing pressure, some have started to question whether China will continue its economic rise.

These calls are often premature and disregard the more interesting questions about the trends in Chinese economic policy – namely, what its political–economic system will look like several decades from now. For now, the signs point to continued government control over the economy, and a backtrack in the liberalization of certain sectors when the government feels that economic stability is threatened. As with other areas of China’s policy-making, ambiguity prevails, official data remain opaque, and little official explanation is given about the direction that China will take. It is therefore essential for the EU and its member states to monitor closely developments in China and to maintain a comprehensive perspective, so as to find links between Chinese policies and activities in various fields at an early stage.

Whither Chinese Institution-building?

In terms of global and regional institution-building, China is not yet finished. There have been reports that China and Russia, and the BRICS countries as a group, are seriously considering setting up their own credit rating agency. The BRICS countries are unhappy that the most important rating agencies are all American and have pointed to the conflict between the political interests of the United States and the ‘independence’ of the rating agencies. Political considerations and neo-liberal norms are seen to feed into decisions about the rating of countries or companies and these are viewed by the BRICS nations as benefiting US foreign policy. A BRICS rating agency would reduce the dependence on these existing US agencies and could potentially decouple the interests of US foreign policy from ratings.

The IMF is another institution that some believe will soon be challenged by a competitor created by China or BRICS. The CRA, which was recently launched by the BRICS nations, fulfils a similar role, but, as mentioned earlier in this report, is not large enough to be seen truly as an alternative. The amount of funds that the CRA would require to create a serious competitor to the IMF makes this an unlikely proposition.

131 See, for example, Russia Insider, 3 April 2015. The Chinese agency Dagong Global Credit Rating was established back in 1994, but its reputation remains disputed.
Also, institutional mechanisms such as surveillance and conditionality have not been established, and rapid-response procedures to handle a fast-developing financial crisis are lacking. The same can be said about ‘Asia-only’ initiatives, in particular the Chiang-Mai Initiative Multilateralization (CMIM), a currency swap arrangement among the ten ASEAN countries, China (including Hong Kong), Japan and South Korea. Furthermore, the Chinese efforts to include the renminbi in the SDR do not suggest that there are currently plans to launch a competing institution. Lacking a viable alternative, it is more likely that China will continue its efforts to alter the IMF and its policies so as to benefit better China’s own ambitions and interests. Established powers, including those in Europe, should make use of this opportunity to press China to conform to existing standards, but they will be hard-pressed to do so without reforming the institution as a way to maintain its legitimacy.

Similarly, the pressure on the OECD DAC and its definition and standards for ODA will continue to be put under pressure. The Chinese are unlikely to join the OECD and will instead apply pressure on the OECD DAC members by offering a competing, and for certain recipients more attractive, form of development cooperation. China’s growing engagement in African countries – traditionally the focus of European ODA efforts – has stirred heated European debates in politics and academia about the linking of trade, investment and development. Many European governments – including the Netherlands and Denmark – have in recent years promoted so-called ‘economic diplomacy for development’, wherein assistance efforts should also benefit the domestic private sector. Intensifying competition, particularly from China, has contributed to these trends.

Equally important is the future of the new AIIB and the NDB. As the AIIB was built largely by the Chinese and China has a greatest share of the votes, this will likely be the main focus of Chinese multilateralism. The NDB is important for China as a sign of BRICS cooperation, and, if only for that reason, the bank is unlikely to fall into irrelevance. Nonetheless, the AIIB is seen by China – and, perhaps more importantly, the rest of the world – as the test of China’s ability to be a responsible stakeholder and leader in the area of global economic governance. As such, the European countries that are members of the bank should appreciate the AIIB as a central tenet of multilateralism in Chinese foreign economic policy. Close coordination among European capitals will be important to present a united front and thereby have more influence in the operation of the AIIB. Furthermore, the European members should explore the costs and benefits of potential US and/or Japanese participation. Japan, in particular, could provide a regional counterweight to the Chinese.

As another central tenet of Chinese foreign policy, and one with important domestic consequences, the ‘One Belt, One Road’ initiative should be closely considered by the EU and its member states. The scale and ambitions of this initiative mean that it will continue to feature large in China’s foreign policy in the coming decades. As evidenced by the launch of the Connectivity Platform, the EU has recognized the importance of
creating a common framework for European cooperation with China on the Silk Road. As transport is a shared competence and the EU also has a mandate for this, it is important to keep track of all the developments relating to these initiatives.

There are still big steps to be taken in Europe regarding the coordination and linking of domestic and EU policies and strategies. The Connectivity Platform offers the various EU member states a foundation and common framework around which they can further develop their strategies vis-à-vis China and the Silk Road. With a project as expansive as the Silk Road initiatives, there is ample opportunity for European countries to hurt each other’s interests unintentionally, or to start projects unilaterally that do not link up well with those in other countries and provide little benefit to Europe.

Countries that are starting to study the implications and potential benefits of the Silk Road should share their findings with fellow EU member states and spur these countries to do the same. The Netherlands appears to be a front-runner in working towards the establishment of a Silk Road platform to discuss opportunities and challenges between policy-makers and private-sector representatives. In addition, the Silk Road Headlines, a weekly newsletter, represents a modest attempt to monitor developments and to spur debate. Such institutionalized platforms at the EU and member-state levels will help to create a more detailed picture of the interests in and consequences of Silk Road projects around Europe. Consider, for instance, the ports of Rotterdam and Piraeus: developments in the latter may harm the interests of the former, but with good communication from an early point, the EU and its member states can together find the best possible solutions. Investments in infrastructure that carry long-term economic interests for countries are more likely to cause friction between EU member states than some of China’s other activism. A broad view of China’s activities, with good communication between European countries about strategic interests – including the promotion and protection of open rules-based markets – and how domestic and common goals can best be achieved, is necessary in order to protect European interests and ambitions.

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132 The Chinese media was quick to report about this initiative of the Netherlands Institute of International Relations ‘Clingendael’, which was endorsed by the Dutch Ministry of Foreign Affairs: see http://news.xinhuanet.com/english/2015-08/21/c_134542535.htm.


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