China-EU Trade Relations

--The period after 1975

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# China-EU trade relations - The period after 1975

**Title**  China-EU trade relations - The period after 1975

**Author**  Xue Leng

**Abstract**

The aim of this thesis is to analyze China-EU trade relations with focus on the period after 1975, when the diplomatic relations between China and EU developed. The research questions are (i) what is the driver in the development of China-EU trade relations? This question is subdivided into two questions: how do economic factors impact on China-EU trade relations and how do political factors influence China-EU trade relations? (ii) what are the existing problems in the current China-EU relations? (iii) what are the future prospects?

To carry out the research questions and fulfill the aim of the paper, a qualitative and quantitative method has been chosen in order to interpret and understand China-EU trade relations. The
theoretical framework of this study is neo-realism and neo-liberalism with particular attention focusing on political issues and economic issues respectively.

A number of conclusions can be drawn from research. First, China-EU trade has developed very rapidly. Trade relations between the two sides are good. They are the third largest traders with each other. Secondly, the momentum for the development of China-EU trade relations is rooted in their common interests in both the political and economic fields. Thirdly, the prospect of China-EU trade relations is promising. These factors include (i) the establishment of a foundation to promote the healthy development of China-EU trade (for example, a set of legal framework provides both sides with the legal basis for their economic relations); and (ii) the prediction of future political and economic environment as favorable to the development of China-EU trade relations.

All factors show optimistically that China-EU trade will continue to prosper. The China-EU trade relationship is not without friction and the author theorizes that there are some potential danger factors; such as the Taiwan issue and trade disputes that may shadow the future development of China-EU trade relations and cannot be overlooked. At the end the author puts forward four suggestions to promote the further development of China-EU trade relations: (i) maintain the existing high-level of exchanges such as the annual EU-China summit; (ii) set up a warning mechanism to prevent trade disputes escalating; (iii) provide a method for establishing negotiations; (iv) prevent the politicizing of trade relations, for example, do not connect human right issue with trade relations. Unrelated issues should be addressed separately.

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Keyword
the EU, China, trade, China-EU trade relations, dumping, anti-dumping policy, the WTO, neo-realism, neo-liberalism
Abstract

This paper is the master-thesis to the Master program in International and European Relations at the Department of Management and Economics of Linköping University.

As the title indicates, the aim of this paper is to analyze China-EU trade relations with focus on the period after 1975, when the diplomatic relations between China and EU developed. The research questions are (i) what is the driver in the development of China-EU trade relations? This question is subdivided into two questions: how do economic factors impact on China-EU trade relations and how do political factors influence China-EU trade relations? (ii) what are the existing problems in the current China-EU relations? (iii) what are the future prospects?

To carry out the research questions and fulfill the aim of the paper, a qualitative and quantitative method has been chosen in order to interpret and understand China-EU trade relations. This study is based mainly on secondary sources including literature, official documents such as publications from the EU, articles and material from newspapers/internet in the forms of document analysis, literature review and existing statistics research. The method of case study is also applied to this study for examining a specific instance or event arising in China-EU trade relations and providing in-sights and illumination.

China-EU trade relations are an intricately social phenomenon, and changes in the nature of China-EU trade relations are determined by changes in the political and economic environment. Therefore, the theoretical framework underlying this analysis of China-EU trade relations is neo-realism and neo-liberalism with particular attention focusing on political issues and economic issues respectively.

A number of conclusions can be drawn from research. First, China-EU trade has developed very rapidly. Trade relations between the two sides are good. They are the third largest traders with each other. Secondly, the momentum for the development of China-EU trade relations is rooted in their common interests in both the political and economic fields. Politically, China and the EU share the same vision of the world order. Both of them advocate the multi-polarization of the world. Close China-EU trade relations can offer a ground for further cooperation on international and regional security issues of mutual concern, including combating terrorism and
nonproliferation. In the perspective of economy, China and the EU are strongly complimentary to each other. China-EU trade results in a ‘win-win situations’ beneficial to both sides. Thirdly, the prospect of China-EU trade relations is promising. These factors include (i) the establishment of a foundation to promote the healthy development of China-EU trade (for example, a set of legal framework provides both sides with the legal basis for their economic relations); and (ii) the prediction of future political and economic environment as favorable to the development of China-EU trade relations.

All factors show optimistically that China-EU trade will continue to prosper. The China-EU trade relationship is not without friction and the author theorizes that there are some potential danger factors; such as the Taiwan issue and trade disputes that may shadow the future development of China-EU trade relations and cannot be overlooked. At the end the author puts forward four suggestions to promote the further development of China-EU trade relations: (i) maintain the existing high-level of exchanges such as the annual EU-China summit; (ii) set up a warning mechanism to prevent trade disputes escalating; (iii) provide a method for establishing negotiations; (iv) prevent the politicizing of trade relations, for example, do not connect human right issue with trade relations. Unrelated issues should be addressed separately.
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Acronyms and Abbreviations

APEC  Asia Pacific Economic Cooperation
ASEAN  the Association of South East Asian Nations
CEECS  Center Eastern European Countries
EC     European Community
EU     European Union
FDI    Foreign Direct Investment
GDP    Gross Domestic Product
GNP    Gross National Product
NATO   North Atlantic Treaty Organization
UN     United Nations
US     United States
WTO    World Trade Organization
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CHAPTER 1: INTRODUCTION

1.1 Defining the Problem

This study focuses on a dramatic development in trade between the European Union (EU) and China after 1975, when diplomatic relations were being established. The definition of this period is not accidental, because the year 1975 is a milestone symbolizing the normalization of China and EU bilateral relations. Before 1975, China-EU trade was carried out only through the individual member states of the EU trading with China. This paper intends to analyze China-EU trade relations at the EU level.

The value in studying the China-EU trade relations can be measured by the importance of China and the EU in the world. China and the EU are nations with growing power and influence on international affairs. The EU is a highly developed industrialized region, and China is a fast-growing developing country. The EU currently is the world’s second largest single market and accounts for 40% of international trade (including the trade among EU member states). The EU is the world’s prime source of Foreign Direct Investment (FDI) outflows as well. Although its trade proportion in international trade currently lags behind of the EU, the rank of China is gradually increasing. “China is already the world’s seventh largest trader, the second largest recipient of FDI” after the US. China’s growing political and economic weight has increased its importance in international society. China and the EU play an important role in Asia and in Europe.

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1 Trade, as referenced in this paper, includes primarily import and export. However, since aid, trade and investment have strong links, and they are mutually beneficial, it is inevitable that aid and investment will be discussed in some parts of this paper.
2 The EU, an economic and political organization, is the progeny of the European Community (EC). On April 18 1951, France, Germany, Italy, Netherlands, Belgium and Luxembourg signed the treaty of the European Community of Steel and Coal (ECSC), which entered into force on July 25 1952. On March 25 1957, the above-mentioned six countries established the European Economic Community and the European Atomic Energy Community. In 1965, the three communities merged into one European Community. The Maastricht Treaty entered into force November 1, 1993, and the term ‘the EU’ was replaced progressively with the term ‘the EC’. In this paper, the use of the terms of ‘the EU’ and ‘the EC’ are not strictly distinguished, and the term ‘the EU’ is used most often.
3 EC Delegation in Beijing. [http://www.delchn.cec.eu.int/cn/eu_guide/Trade_Relations_Multilateral.htm](http://www.delchn.cec.eu.int/cn/eu_guide/Trade_Relations_Multilateral.htm)
respectively, even in the world. They are becoming two positive participators in the
process of multi-polarizations and economy globalization. Their role in international
relations should not be overlooked.

China and the EU are becoming two important global leaders in today’s world. There
exists the necessity for mutual cooperation between them. The future of the EU depends
on the further integration and reform of the EU itself. For instance, the EU needs to
continue its integration process, deepen its institutional reformation, develop its Common
Foreign and Security Policy, and put the fifth enlargement plan into effect, as well as to
strive for more credits for the common currency, the Euro. The EU especially needs to
expand and to enhance its presence, including access to more markets, in the world
especially in Asia. The report “Europe and Asia: A Strategic Framework for Enhanced
Partnerships” states that “the EU is in need of other markets and China is potentially the
biggest”.\(^5\) In all these aspects, it is necessary for the EU to obtain mutual support, mutual
cooporation from other regions and countries including Asia and China. As for China, the
EU remains every bit an important partner and supporter for her ongoing reform process
and her integration with global economy. In a word, both sides have a significant stake in
one another’s development.

Since the end of the cold war in the early 1990s, the EU has seen the opportunity to
realize its dream of a wider Europe and to counterbalance the restrictions from the US. In
this respect, the EU promulgated strategic relations with China. The EU’s policy paper
issued in 2003 pointed out that China is one of the EU’s major strategic partners and
China-EU relationship is a maturing partnership.\(^6\) A series of documents set by the EU,
such as “A Long Term Policy for China-Europe Relations” in 1995, “Building a and
Comprehensive Partnership with China” in 1998, indicate that China-EU trade relations
have now entered a new phase. Owing to the positive impetus by these polices, the
China-EU relations have developed more rapidly than ever before. For instance, the total


\(^6\) EU (2003), A Maturing Partnership-Shared Interests and Challenges in EU-China Relations.
two-way trade between the EU and China has increased from 11.61 billion US Dollars in 1991 to 48.863 US Dollars in 1998 (see table 3). The fact that China’s rapid economic development in the past twenty years has had a significant impact upon EU-China trade relations is worth noticing.

Although China-EU relations have been developed rapidly in the last two decades, there are still untapped potentials for increased trade relations between these two countries. For instance, China shared only 6.8% of the EU’s total imports and 2.7% of the EU’s total export in 2000.\(^7\) To develop further the trade potentials between China and the EU, it is necessary to improve the mutual cooperation by tackling existing problems in bilateral trade relations.

This paper attempts to review the history of the China-EU relationship and its current status and to examine the existing problems and issues. Hopefully this thesis will contribute to the improvement of the China-EU trade relationship.

### 1.2 Aim and Research Questions

The overall aim of the present study is to analyze the China-EU trade relations since 1975. More specifically, the objectives of this thesis are:

- Review the current literature and policy papers related to China-EU trade relations.
- Pinpoint the main factors determining or influencing the direction and scope of the relationship between the two countries.
- Explore the tendency of the future development of the China-EU relationship.

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This thesis looks at the issues both from the point of view of a broad theoretical framework and from the perspective of the macro social contexts. The analysis is based mainly on the assumptions of two theories of international relations, the Neo-realism and the Neo-liberalism.

The research questions are:

(i) what is the driver of the development of China-EU trade relations?
   This question is subdivided into two questions:
   (a) how do economic factors impact on China-EU trade relations?
   (b) how do political factors influence China-EU trade relations?
(ii) what are the existing problems in the current China-EU relations?
(iii) what are the future prospects?

1.3 Methodology
To conduct the present study, three complementary methods are employed. First, a review of the relevant available literature on the topic provides the foundation of the methodology of the study. According to Blaxter et al. (2001) “a literature review is a systematic, explicit, and reproducible method for identifying, evaluating, and interpreting the existing body of recorded work…” and “that good literature reviews go beyond the stage of simply listing sources to offer an analytical study of the area, through which you can develop your own position, analysis and argument”. The author believes that a literature review is able to provide a knowledge base of the topic and provides a picture of the current relationship between China and the EU. This provides a basis for understanding, critical examination and discussion of the development process of the China-EU trading relationship. Secondly, an analysis of secondary data was conducted on available statistical data, relevant documents, and official/media publications. To complement the above-mentioned methods, case studies were also employed to gain a better understanding of the context in which the issues occur.

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1.3.1 A Qualitative and Quantitative Approach

This paper has multiple purposes: to provide a picture of the current trade situation between the EU and China, to identify the main factors determining, influencing and encumbering the direction and scope of the relationship between the two countries, and to explore the development prospects of trade between the two countries. Hence this research is kind of explanation research, which “builds on exploratory and descriptive research and goes on to identify the reason something occurs”\(^9\). A holistic approach was emphasized in this study, in which, both qualitative and quantitative methods were used in a complementary manner. The combination of qualitative and quantitative approach, which aims to interpret and understand a phenomenon in its context through a detailed examination of text and statistics, fits perfectly with the objectives of this paper.

China-EU trade relations are an intricately social phenomenon, and changes in the nature of China-EU trade relations are determined by changes in the nature of society. During the last decades, the context and imperatives for bilateral relations have changed considerably due to various factors such as the end of cold war, the globalization of the world economy, the enlargement of the EU, and the reform of Chinese economic and political system. Taking context into account avoids the possible shortcomings of viewing the China-EU relationships in a vacuum. “When a researcher removes an event, social action, answer to a question, or conversation from the social context in which it appears, or ignores the context, social meaning and significance are distorted”\(^10\). Following a qualitative and quantitative approach, the objectives of the study will be served. The combination of qualitative and quantitative approach is less vulnerable to inherent to the particular method. For example, the qualitative method is often criticized as unrepresentative, unreliable, and incomparable because its data is ‘soft’ and intangible, therefore one is unable to generalize conclusion from the findings. The major drawback of the quantitative method is the research cannot conduct detailed examinations of events that arise in social life. The combination of these two methods can solve their respective limitations perfectly, and contribute much to this study.

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\(^10\) Ibid, p.146.
In this study I used the qualitative method to interpret the context of China-EU trade relations to provide a detailed picture. To make the data more reliable and comparable, I also relied on statistical data. Different types of data provide cross-data validity checks. The volume of detailed written notes wrote when I recorded data is the other way to guarantee the trustworthiness of this study. The reader can check references and sources.

The limitation of this study is that this study is based mainly on secondary sources. The data collected may be superficial and cannot examine a specific instance and illuminate a general problem. This study used the case study (see table 2: Example 1 and table 5: Example 2) method as the means of reducing the disadvantage from using secondary sources. The case study focuses on a particular situation or event, so that one could achieve a full understanding and in-sight of the phenomenon as possible.

### 1.3.2 Data Conduct

The data used in this paper is based on available data up to February 1, 2004. Most of data is in the form of text, written words. The numerical information in this paper is supplementary to the textual evidence. The methods of the study are the forms of document analysis, literature review, the collection of existing statistics and case study.

The study of China-EU relations is a rather new topic. Thus, a big effort was taken to select the materials. In this study, the materials are course literature, academic journals, books, official documents, and computer files, which provide insight into this subject. Course literature includes course books and course lectures. The remainder of the materials was collected via university library, public library, newspaper, and the Internet. All selected materials are organized into two categories (primary, secondary) by their source. Primary source materials are those written by someone who is able to give a first view on the subject written. For example, the official documents collected from the EU’s homepage and China’s official website (National Bureau of Statistics of China, Chinese Customs Administration, and Ministry of Foreign Affairs of China), and the speeches on China-EU trade relations made by the EU trade Commissioner Pascal Lamy and by
Chinese Prime Minister Wen Jiabao were sorted as primary source. These sources are important for the review of the empirical work within this study. Secondary sources were used to locate other documents and references related to this study. For example, the article ‘China-European Union Bilateral Trade: in Retrospect and in the Future’ written by Tong Jiadong, which examined China-EU bilateral trade during the period from 1975 to 1997 and analyzed the factors encumbering the development of the two sides’ trade was categorized into secondary sources. These sources were used for literature review, which provides an overview of the China-EU trade relations, and gives a picture of the trend of the China-EU trade relationship in the future by analyzing and comparing them. A few examples are closely examined in this paper. The criterion for selecting examples was based on the ability of the example to clarify and deepen understanding.

In this thesis, besides qualitative data, I used statistical data to try to point out the development trends of China-EU trade and the relationship between trade and political events. During the process of gathering trade statistics, to make the data more reliable, I attempted to collect and compare trade statistics from both Chinese side and the EU side. I tried to contact the EU information center, the European Commission Delegation in Beijing and a number of libraries. The EU information center replied that they would charge for subscribing information. The European Commission Delegation in Beijing and the libraries suggested I get in touch with the Chinese Customs Administration. I also visited the World Trade Organization’s (the WTO) homepage and examined ‘International trade statistics 2003’. There were limited trade statistics available on China-EU different sections (for example IT section, service section and textile section). In the end I only got a complete China-EU trade statistics from Chinese Customs Administration with help from my friend, who works for the Chinese embassy. Therefore, this thesis depended mainly on statistics from the Chinese side.

The documents for doing this study were selected using two methods. The first method was to select documents based on the perception that they are central to the debates surrounding the China-EU trade relations. These documents were books and journal articles written by important people or collected by authoritative organizations such as
the World Bank, the WTO, EU publications, and Chinese Academy of Science. Second, the Internet is the other important source of the remainder of the documents selected. These searches used various databases from the Internet. Among those general databases used are those within the EU website, Libraries, and so on.

In a qualitative and quantitative research, the selection, code, analysis, and interpretation of data blends together. The process of analysis and interpretation of data starts with the beginning of coding data. In the process of analysis and interpretation of data, I wrote notes to record comments and research strategy. Writing analytic notes helped me in re-thinking the data. ‘The analytic memo forges a link between the concrete data or raw evidence and more abstract, theoretical thinking’\(^{11}\). In evaluating documents, I attempt to consider the complex relationship between document, author, and the social, political, and historical environments. A hermeneutic approach was used in the process of document analysis.

1.4 Review of Relevant Literature

1.4.1 Theoretical Literature

Detailed analysis of theoretical approaches towards China-EU trade relations is presented in Chapter 2.

A fundamental book referenced for this paper is *The Globalization of World Politics*\(^{12}\) by John Baylis & Steve Smith. This book provides an overview of contemporary world politics and a comprehensive summary of the main theoretical approaches available to explain contemporary world politics. This book is particularly helpful in understanding neo-realism and neo-liberalism in the context of world politics, world economy and international trade.

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\(^{11}\) Ibid., p.424

Another book ‘Theory of International Politics’\(^{13}\) by Kenneth Waltz in 1979 is the benchmark for Neo-realism. This book analyzes the structure of inter-state relations, which is characterized by anarchy. How the states behavior in the ‘self-help’ system is discussed, which helps to understand the current trade relations between the EU and China. The collection of essays, *Theories of International relations*\(^{14}\), is a good reference on liberal international and neo-realism. This reference provided theoretical support for this study.

1.4.2 Empirical Literature

There are some previous works concerning the issue of EU-China trade relations, which deserve some mention here.

The book, entitled ‘The EU long-term policy towards China and China-EU economic and trade relations’\(^{15}\) by Qiu Yuanlun and Wang He, gives an overall introduction of the EU long-term policy towards China and analyzes the historic review of the development process of EU-China economic trade relations in general. This book investigates the trade relations between China-Germany, China-Great Britain, China-France and China-Italy in detail. The authors point out the development of economic and trade relations between the two sides as the basis of the EU re-focus on China. This reference also puts forward several suggestions for China and individual member states of the EU on how to solve the current disputes between them, therefore promoting their bilateral relations.

Pan Qichang in the author of ‘European International Relations’\(^{16}\). This book is useful for understanding the EU’s foreign policy. The author analyzes the relations between the EU and Asia and its strategy policy towards Asia. In this book he argues that the future of EU-China cooperation is promising.


\(^{15}\) Qiu Yuanlun & Wang He (1999), *The EU Long-term Policy Towards China and China-EU Economic and Trade Relations*. Social science literature press.

\(^{16}\) Pan Qichang (2001), *European International Relations*. Economic science press.
The weaknesses existing in the current study of China-EU trade relations are mainly:
1. The theoretical frameworks and methods adopted in the research have not been studied and summarized.
2. There is a lack of systematic and in-depth study of the China-EU trade relations.
3. The forecast for EU-China relations has not been supported with empirical evidence.

1.5 **Structure of the paper**

**CHAPTER 1. ‘INTRODUCTION’**: This chapter focuses on defining the problem. The outline of the research questions and the objectives of this study are provided. The methodology applied to this study is described.

**CHAPTER 2. ‘THEORETICAL FRAMEWORK’**: This chapter sets out the theoretical underpinnings to this critical evaluation, in which the theory of neo-realism and neo-liberalism will be examined. This chapter comprises a review of these two theories and attempts to analyze China-EU trade relations within the theoretical framework.

**CHAPTER 3. ‘BACKGROUND AND ANALYSIS’**: In this chapter a historical review of China-EU trade relations is provided. It is now generally accepted that the change of bilateral relations cannot be adequately understood in isolation from the social framework within which it takes place, so the author in this chapter depicts first the development of Asia, China, and EU, which sets the background for China-EU trade relations. The author will try to identify and analyze the motives of China the EU as they actively adjusting their attitude towards each other. An analysis of the total trade volume between China and EU will be provided at the end of this chapter.

**CHAPTER 4. ‘THE CURRENT SITUATION’**: This chapter intends to examine the current situation with focus on the factors of trade balance and China’s WTO membership, the antidumping dispute, the negative impact of EU enlargement and the issue of human rights that are shaping and influencing China-EU relations.
CHAPTER 5. ‘THE PROSPECT ANALYSIS’: This chapter predicts the prospect of China-EU trade relations by analyzing the future social context, such as future political and economic environment.

CHAPTER 6. ‘CONCLUSION’: This chapter draws the final conclusions and makes suggestions for further developing China-EU trade relations.
CHAPTER 2: THEORETICAL FRAMEWORK

2.1 Introduction

The basic problem facing a researcher, who tries to understand a certain issue or conducts a research, is how to select the unit of analysis most relevant to the problem from the millions of possible facts, and how to find the starting point. At that moment, we have to resort to a theory outlining for us specific actors, processes, and levels of analysis. Theory can provide guidance for developing a better understanding and to formulate a better solution. Baylis and Smith think of theory as a simplifying device that helps one to decide the facts that are the most important. To avoid being driven by ephemeral incidents and breaking news, and to get a firm grasp of the certain events from different lenses, alternative theoretical perspectives are examined in this chapter.

The core question of this paper is: what drives and explains the development of China-EU trade relations? As we know, a country’s foreign policy takes the factors of economic, politics, security, environment, and human rights into account. I assume that China and the EU’s preferences and interests in developing their bilateral trade relations are driven by the concerns of political strategy and economic gains. In order to explain how and why these countries came to have particular preferences, I used the approaches called ‘neo-realism’ and ‘neo-liberalism’, two of the dominant theories of International Relations. The reason to choose these two theories is that I study both political and economic aspects and these two theoretical perspectives deal with these aspects in different ways. Neo-realism puts an emphasis on politics and neo-liberalism stresses economy. Their differing estimates of China-EU trade relations may provide the reader a more comprehensive picture concerning this issue. In the first section I am going to review the core assumptions underlying neo-realism and see if neo-realism is relevant for understanding contemporary EU-China relations in general and EU-China trade relations in particular. In the second section I will do the same for neo-liberalism.

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2.2 Neo-realism

There are various strands of neo-realism, stressing different aspects of the approach. This paper will apply it as a consistent approach, as done by representative scholars such as Kenneth Waltz, Joseph Grieco, John Mearsheimer, and Robert Jervis. Two important works, ‘Man, the state and war: a theoretical analysis’ in 1965 and ‘Theory of International Politics’ in 1979, done by Kenneth Waltz, have become the benchmark for neorealist. Neo-realism “provides the most powerful explanation for the state of war which is the regular condition of life in the international system”.\textsuperscript{18} Neo-realism depicts the characteristics of the international system as a whole, and explains how these characteristics affect the behavior of individual states.

Neo-realism consists of a few key assumptions. First, that the most important actors in world politics are territorially organized entities, for example states and city-states (Waltz 1979). “Other actors such as multinational corporations or international organizations all have to work within the framework of inter-state relations.”\textsuperscript{19} Second, the international system is characterized by \textit{anarchy}, which is the primary force shaping the motives and actions of states (Waltz 1979:79-128; Burchill 2001:70-102). Neo-realists claim that conflict and war are unavoidable because of anarchy. In anarchy, there is an absence of any effective authority above the state that can ensure their compliance to agreements and norms. As a result, the international system is a \textit{self-help} system, with states trying to maximize their national interests in order to gain national security through \textit{struggling for power}. The mechanism for the struggle for power is \textit{the balance of power}. States tend to balance their rivals domestically, by acquiring greater military and economic power, or by building alliances with stronger powers.\textsuperscript{20} Waltz and Mearsheimer state “in international politics, overwhelming power repels and leads others to try to balance against it”.\textsuperscript{21} But Amitav Acharya argues that security can only be achieved in a limited

\begin{itemize}
\item \textsuperscript{18} \textit{Ibid.} 141.
\item \textsuperscript{19} \textit{Ibid}. 4.
\item \textsuperscript{21} \textit{Ibid}.98 cited from Waltz (1991) and Mearsheimer (1990)
\end{itemize}
way, because of the operation of the "security dilemma", whereby attempts by any state to improve its security by acquiring the means of power provokes other states to follow suit, thereby rendering the initiating state as insecure as before.\textsuperscript{22} Neo-realists hold that international institutions affect international order only marginally. They argue that institutions are creatures of self-interested great powers, and what really matters is the balance of power.\textsuperscript{23} The weakness with this approach is that it only stresses the importance of the role of structure in the international system as the key determinant of state behavior, without taking their domestic character into account. For instance, many neo-realists believed the bi-polar system is stable, but the end of the cold war endangers the neo-realism position in international relations’ theories since it fails to provide a reasonable explanation without considering the former Soviet Union’s domestic features.

Neo-realism would suggest that both the EU and China’s foreign trade policy toward each other reflects their understanding of the changing balance of power. After the end of the Cold War, the structure of the international system has been changed dramatically, from bipolarity system to single-polarity system, and to multi-polarity system with the rise of the EU, China, Japan, and so on. Neo-realism tells us that the balance of power involving more than two actors tends to be inherently unstable because of the difficulties in making a reliable calculation of the balance. The US had played the role of hegemon during and after the Second World War, and the end of the Cold War further firmed its hegemonic status. However, by the 1970s because of the economic success in Europe and Japan, and in recent years the rise of China, the downward spiral of the US’s own economy, and the enormous military expenses of the Iraq war, the capacity of the US to maintain its hegemonic status is in question. There would be a shift in the balance of power if the US did lose its hegemonic status. This may explain why the alliance between the EU and China should be strengthened both economically and politically. And the development of the relations between China and the EU also has strategic meanings. In the period of Cold War, in order to contend with the threat from the Soviet Union, Europe

\textsuperscript{22} Amitav Acharya, “International Relations Theory and Cross-Strait Relations”.

\textsuperscript{23} Ibid.
and the US have coalesced politics and the military. After the end of the cold war, with the changes in the international environment leading to changes in their foreign strategies, EU-US relations has entered into a new era of adjustment. The EU, along with its growing political and economic power, would like to shake off the control of the US and seek economic and political independence. The basic idea of the EU’s diplomatic strategy is to seek a new strategic partner, to strengthen its presence in international affairs and to increase its ability to contend with the US. Keeping this in mind, the rise of the relative weight of China in the world politics and economy makes China attractive to the EU. As to China, the US has posed a number of political and economic restrictions on China since the US believed in the ‘China threat’ in recent years. Thus, the development of relations with the EU is in the best interests of China. Regarding the current strength of China and the EU, separately they are not as strong as the US. However, it would be another story if they could cooperate together. For example, on some international issues they could support each other to counterbalance the US. Both China and the EU stand on one common ground that they both dislike hegemonism and dislike the US interference. As Waltz and Mearsheimer state “in international politics, overwhelming power repels and leads others to try to balance against it”.24 In addition, China-EU relations could counterbalance US-Japan relations in Asia as well. The US always maintained close relations with Japan and East Asia through the Asia-Pacific Economic Cooperation (APEC). Developing China-EU trade relations can be seen as a counterweight to US-Japan in Asian region. Within a neorealist context this would be translated into the creation of a balance of power in a region.

Neo-realists emphasize that the inherently competitive nature of the international system requires states to achieve relative gains in international politics. They argue that policymakers will largely be concerned with ‘do we gain more from this than other states?’, rather than ‘do we gain from this?’. Mercantilists also depict the world economy as a stage for inter-state competition for power.25 But what is ‘power’? The old notion of

24 Ibid.
‘power’ indicates mostly military power. Neo-realism has extended its definition as the capabilities of states, remarking by the following items: “size of population and territory, resource endowment, economic capability, military strength, political stability, and competence” (Waltz 1979:131). Thus relative gains are gains in capabilities. Along with the economic globalization, the EU, as an independent economic bloc, would never easily give up the market shares in the Asia region including China. Especially, in its competition with the US and Japan, giving up a potential and vigorous market in the world means a disadvantage in the competition. “One country’s gain was another’s loss”.

In other words, more for one actor means less for another. By reflecting neo-realism views that power is zero-sum, if the EU strengthens the economic and trade relations with China it has a strategic importance and vice versa.

Although neo-realists agree that international cooperation is possible, they rather see international cooperation as “hard to achieve, difficult to maintain”. This is so because, as Waltz claims, “states concern of relative gains than absolute gains”, which confine the willingness of states to cooperate. The trade disputes between the EU and China would be a good example of ‘relative gains problem’. The EU wanted a greater ‘market share’ in China, so that it established a series of development policies towards China to promote trade between them. But at the same time the EU also fears that China may achieve relatively greater gains from their cooperation, and China, as a result, will be stronger than it own in relative capabilities; and, finally, that China with increasing power could become the more dangerous rival in the future. ‘Today’s friend may become tomorrow’s enemy’. With this fear in mind, the EU has set up instruments to restrict the competitive challenge from China. The European Community introduced an extensive system of so called voluntary export restraints. Clothing, textiles, cars and steel were the sectors most frequently and extensively protected by these instruments. Of course, China has adopted

corresponding measures as a response. The continued ‘trade war’, to a certain extent, proves the assumption of neo-realism on that when states always consider their relative gains international cooperation is hard to maintain.

From the neo-realism perspective, China-EU trade relations have a favorable political environment for promoting their development. However, there are some obstacles to trade that cannot be overlooked.

2.3 Neo-liberalism

Neo-liberalism shares some of the same views on international society with neo-realism. For instance, both agree that the system of international society is anarchic. The differences between the two are reflected in how neo-liberalists disregard some of the neo-realism’s claims and emphasize new factors. Two especially important works in the field of neo-liberalism are worth to stressing here. The first one is After Hegemony: Cooperation and discord in the World political Economy (Keohane 1984). The other is Power and Interdependence (Keohane and Nye 2001, third edition). These two books provide a rich theoretical approach to understand international cooperation and international political economy and to understand the relationships between economics and politics.

Neo-liberalism encompasses four propositions. First, states not only engage in conflict, but they can also engage in co-operation (Keohane, 1984). Second, states are main actors in international relations. However, the importance of roles played by non-state actors (for example international institutions, multinational companies, NGOs, and so on) in the world arena cannot be ignored (Burchill,S. & Linklater,A. eds., 2001). Third, states are interdependent, and they can be concerned with absolute gains (Burchill,S. & Linklater,A. eds., 2001; Keohane and Nye, 2001). Fourth, anarchy does not mean “no governance” but means “no government”. (Burchill,S. & Linklater,A. eds., 2001)
Neo-liberalism contributes a great deal to the discussion of economic aspects of international relations. Its tradition is the free market, one in which countries gain from specialization by utilizing their own natural advantage, resources, and endowments. The development of China-EU trade relations results from the prevalence of market economy, which is imaged by Adam Smith as an invisible hand that makes the distribution of goods and services more efficient and equitable across the world economy.\textsuperscript{29} China and the EU trade relations, from neo-liberalist perspective, are determined by the relative economic performance of both sides, by the degree of complementarity and by mutual benefits. Undoubtedly, China and the EU are highly complementary economically. Both China and the EU see the advantages of mutual co-operation. China, with a large population, has an abundantly cheap workforce. The Chinese economy has developed rapidly and steadily as witnessed by the world, and her market potential is enormous. However, China limited capital, and the technical level is relatively low compared with the EU. China’s competitive advantage, therefore, rests on labor-intensive products; while the EU’s competitive advantage rests on technology-intensive and capital-intensive products. According to the report of the Ministry of Economic and Trade of China, we can note that China is mainly exporting light industry goods with low technologic content to the EU, and importing machines, transport equipment, and so on from the EU.\textsuperscript{30} China and the EU have everything to gain by strengthening their trade linkage. Neo-liberals, such as Keohane, “believe international relations does not need to be a zero-sum game (relative gains), as many states feel secure enough to maximize their own gains regardless of what accrues to others. Mutual benefits arising out of co-operation are possible because states are not always preoccupied with relative gains”\textsuperscript{31}

Neo-liberals believe that free trade would result economic interdependence, so increasing the costs of war would reduce the likelihood of war.\textsuperscript{32} Globalization is an

\textsuperscript{29} Baylis & Smith (2001). The Globalization of World Politics: an introduction to international relations, 2nd, Oxford University press.
\textsuperscript{30} Chinese economic trade ministry, white paper on Chinese foreign trade in 1998.
\textsuperscript{32} Ernst B. Haas, "War, Interdependence and Functionalism" cited Raimo Vayrynen, ed., The Quest for Peace: Transcending Collective Violence and War among Societies, Cultures and States (Beverley Hills: Sage Publications, 1987).
important character of world today. It means that states are no longer closed units; rather they have become more interconnected than ever, with trade and finances ever expanding across boundaries. Since 1978 the EU and China two-ways trade has increased upward around 20 times. Chinese General Administration of Customs statistics (table 3) shows that in 2001 the total volume of trade between China and the EU was 76,620 million dollars, which has been increased 11% compared with the same period of the previous year. In January – July, 2002, the volume of China-EU trade was 46,230 million dollars, increasing 6.8% compared with the same period of 2001. Until the end of July 2002 the number of the EU investment projects in China was up to 13,283, and agreed foreign capital amounts to 58,700 million dollars and investment 32,570 million dollars. As the two biggest markets in the world, the China-EU trade nexus would benefit both sides’ individual and social welfare, and help attaining their national goals, such as growth, full employment, and price stability. And it is reasonable to believe that both sides are unwilling to promote war between themselves considering the cost of war and the fact that their economic interests interlink together.

Neo-liberalists also hold an assumption that rules and international institutions can help states cooperate, therefore promoting peace and creating harmony among the states. They argue that policy-makers seek to maximize their absolute gains, but meanwhile they worry about cheating. Institutions, neo-liberalists suggested, can solve the problem of cheating by setting up rules. It is said that trade relations between the EU and China have remained stable since the corporation institutions were built. The EU has been a strong backer of China’s entry into the General Agreement on Tariffs and Trade, and supports China’s entry to the WTO. It is certain that membership will accelerate China’s process of trade and investment flows liberalization. Both sides believe that the accession of China to the WTO would normalize and smooth their bilateral trade relations. For the EU, upon entry to the WTO, China will have to cut down import tariffs and open up its markets to EU. In China’s WTO accession deal with the EU, China agreed to reduce import tariffs on over 150 leading European exports. The sharp reduction in tariffs and

34 China-EU agreement on WTO accession. http://www.chinalegalchange.com/Archives/arch0010.html
non-tariff barriers is likely to lead to a surge of the EU’s exports to China. As a consequence, the trade deficit with China would be reduced, and the trade conflicts between the EU and China would be alleviated. For China, the WTO membership could help China to resort to the WTO dispute settlement mechanism to resolve disputes, such as anti-dumping measures that hurt China the most, with the EU. The WTO offers a framework to settle their trade disputations peacefully. Since 1998, the EU-China summit has been set up. It operates annually for exchanging opinions on common concern issues. The establishment of EU-China summit has paved a bridge of understanding. It, therefore, promotes the trade relations of the two sides’.

Through neo-liberalist thinking one gets a picture of democracies being rather "pacific" than autocratic. It has become the major axiom of Western policy, because neo-liberals believe democracies do not fight with one another.35 With the economic development, China is pushing the political reform by perfecting the legal system and promoting democracy. There has been an increase in power for citizens’ political rights at the grass roots level, and over foreign trade by local governments in provinces, municipalities, and cities and towns.

China has actively promoted cultural and ethical progress, constantly improved the people's congress system and the multi-party cooperation and political consultation system under the leadership of the Communist Party of China. China has made great efforts to strengthen the building of democracy at the grass roots level and done a good job in safeguarding citizens' political rights. China's political reform has achieved positive results. The national legislation system has been improved. The supervision over the law enforcement and the judicial organs has been strengthened.36

After the former Soviet Union felt apart, the Communist school is no longer the threat of the Capitalist school. China, who once belonged to the Communist school, is developing toward into a capitalist society with the symbols of the transition from planning economy to market economy and the spread of democracy. The most important momentum for


36 http://www.chinaembassy.org.eg/eng0300/sp020527.htm
China-EU trade is the mutual benefits from the degree of complementarity. All these serve as the foundation of China-EU cooperation and trade.
CHAPTER 3: BACKGROUND AND ANALYSIS

3.1 Introduction

During the 1970s, the comeback of China’s seat in the United Nations (UN), the establishment of official relations between China and a number of the EU member states, and the emergence of the EC as an important international economic entity provided the basis for the further development of the China-EU relations. In 1975, the formal diplomatic relationship established between China and the EU paved the way for developing bilateral trade on the EU level. According to the statistics from Chinese Customs (see table 3), the volume of trade between China and the EU rose from 2.4 billion US dollars in 1975 to 5.3 billion US dollars in 1981. It reached 11.65 billion US dollars in 1986. During this period of time, the trade volume doubled every 5 years. This process was interrupted by the Tiananmen Square event in 1989. After 1991, the bilateral trade between the two economies rebounded again. In 2003 the trade volume between the EU and China had increased more than 50-fold since 1975. Statistics show the bilateral trade volume reached US $ 86.76 billion in 2002. It made China and the EU become each other’s third-largest trading partners.

The most obvious sign of the development of China-EU trade relations is the promotion of policies on trade. In the beginning of the trade relationship the EU took the initiative in promoting China-EU trade relations. The EU has formulated a series of common trade policy towards China since 1975: (i) in 1978, China and the EC signed ‘China-EC Trade Agreement’ to strengthen and legalize their economic and trade relationships, and built up the Joint Committee on Trade Cooperation. This bilateral trade agreement marks a major step forward in China-EU trade relations; (ii) ‘’Agreement on Trade and Economic Cooperation between the European Economic Community and the People’s Republic of China’’ was promulgated by the EU in 1985. This Cooperation Agreement stressed

37 The Major Development of China-EU economic relations by Dr. Zeng Huaqun
http://www.twlcic.com/cm/icm2/Chinaneuro.html
39 Ibid.
40 Ibid.
mainly the cooperation in the areas of agriculture, energy, science and technology, and personal training; in 1994 the EU began to implement ‘a new Asia Strategy’, and afterwards formulated three political documents towards China; (iv) ‘A long term policy for China-Europe relations’ was adopted by the European Commission in December 1995. This strategy paper built up the principles of the EU’s policy towards China and called on the EU to raise its profile in China; (v) in November 1996, the European Commission put forward ‘a New Strategy of the EU on China’ and granted China market economy status; (vi) on June 29, 1998 the European Commission issued a policy paper on ‘Building a Comprehensive Partnership with China’. It proposed “to engage China further in the international community, to support China's transition to an open society based on the rule of law and the respect for human rights, to integrate China further into the world economy, to make Europe's funding go further and to raise the profile of the EU in China”. This document elevated the EU’s relationship with China to the level of equal importance with the US, Japan and Russia, unveiling a mature and stable era in China-EU trade relations; (vii) On September 10, 2003, the EU published a new policy paper on China, “A maturing partnership: Shared interests and challenges in EU-China relations.” The EU stated in this paper that “both sides have to adapt to a fast moving international scene” and, against that background, “the EU and China have an ever-greater interest to work together as strategic partners to safeguard and promote sustainable development, peace and stability. Interests converge on many international governance issues, notably the importance both attach to the role of the UN in physical and environmental security.” Following this EU policy paper on China, China issued “China’s EU Policy paper” on October 13, 2003, which is the first strategic paper on the nation’s policy towards the EU. A number of measures for boosting China-EU economic

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cooperation in the coming five years are outlined in this policy paper. The paper also points out that “To strengthen China-EU relations is an important component of China's foreign policy…China is committed to a long-term, stable and full partnership with the EU… China desires to promote a sound and steady development of China-EU political relations…deepen China-EU economic cooperation and trade.” The issuing of this paper is a further sign of the sound development of China and EU’s bilateral trade relations. (See Appendix 1: Chronology of China-EU relations)

The above-mentioned policy documents serve as the foundation of the development of China-EU trade relations. But, what makes both the EU and China actively adjust their policies towards each other? To understand and interpret this question, we must place the China-EU trade relationship within a larger context. The international situation has been undergoing profound changes since the Second World War. The China-EU trade relation is an intricately social phenomenon and changes in the nature of the China-EU trade relation are determined by changes in the nature of world society. In a globalizing world, the external environment plays a key role. Several developments over the past decades shape China-EU trade relations directly. There are significant developments in Asia, in China, and in the EU. The EU strategic focus from the circum-Atlantic basin to the circum-Pacific basin will be inevitably reflected by the economic growth in Asia and the rise of China. As to China, the importance of the EU in its foreign strategy reflects the increasing influence of the EU in the international stage. In this chapter, I intend to provide a historical context of the development of China-EU trade relations. I will begin by depicting the economic increases both in Asia and China, and the integration of the EU, which is the large and external environment embedding China-EU trade relations. After that, I will try to identify and analyze the driving forces from China and the EU

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47 Asia in this paper is defined as the wider Asian and Asia-Pacific region. Geographically it is divided into Central Asia (Kazakhstan, Kyrgyz Stan, Mongolia, Tajikistan, Turkmenistan, Uzbekistan), North-East Asia (China, Hong Kong SAR, Macao SAR, Japan, North and South Korea, Taiwan), Southeast Asia (Brunei Darussalam, Burma, Cambodia, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand, Vietnam, East Timor), South Asia (Afghanistan, Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan, Sri Lanka). http://europa.eu.int/comm/external_relations/asia/index.htm & http://europa.eu.int/comm/external_relations/asia/country.htm
individual perspective as they actively adjust their attitude towards each other. The analysis of total trade volume between China and EU will be provided at the end of the chapter.

3.2 Economic Growth in Asia

Since the 1960s the economic development in Asia has been a great success story. Rapid economic development has created wealth and economic dynamics in Asia. It is already the world’s largest and most dynamic in terms of Gross Domestic Product (GDP) growth. Currently, Asia is the third largest regional market in the world. It occupies “56% of the world’s population, 25% of world Gross National Products (GNP), and 22% of the world’s international trade”. The economic performance of East Asia is the most outstanding in the Asian region. The per capita income in most of the countries in East Asia has increased eightfold over the last 30-50 years. The emergence of Japan as an important economic power is a significant example. Between the 50’s and the 70’s Japan’s economy increased by average of 11%. In the late 1970s the world discovered an economic miracle in the high growth records of the Asian Newly Industrialized Economies such as Hong Kong, Korea, Singapore and Taiwan. They were called the four little dragons because of their rapid GDP growth with the annually economic development exceeding 6 percent. In the 1980s the world witnessed another economic growth in East Asia represented by China and the Association of South East Asian Nations (ASEAN) countries. The growth continued into the 1990s with a rate of 7%-8%. Hand in hand with the growth of the Asian economy is the increase in the Asian foreign trade. Asia accounts for 22% of world’s international trade and for 21% of EU exports. East Asian financial strength has increased also. At the end of 1995, East Asia has 28 big banks included within the list of World’s 100 biggest banks in the terms of asset. The assets of these 28 banks are $246.979 billion. The development potentiality and strength of Asia economy can hardly be doubted. Although affected by the Asian economic crisis

(1997-1998), some countries in Asia continued to grow economically while other countries like Republic of Korea have since returned to their strong economic growth after the recession in 1999. Growth in Asia improved “from 2.3 percent in 1998 to 6.2 percent in 1999 on the back of strong export growth and a revitalization of domestic demand” \(^{52}\).

The Asian Development Bank stated that the economic growth in the Asia and Pacific region will resume and will continue to be the fastest in the world in 2003 and 2004.\(^{53}\) The forecast for aggregate GDP growth in the Asia and pacific region in 2004 will be upward to 6.1%. (See tendency graph as following)\(^{54}\) The developments of Asia in 2003 confirm this assessment.

**Graph 1: GDP Growth In Developing Asia**

![Graph showing GDP growth in developing Asia](source)

Source: cited from Asian development outlook 2003\(^{55}\)

The positive development of Asian economy is beyond question if the global economic environment remains stable. Asian Development Outlook 2003 stated that “the Asia region will remain a bright spot on the world economic map”.\(^{56}\) The World Bank also estimates that East Asia in one of the world’s most dynamic, resilient and interdependent economic regions. After recovering from the shade of the Asian financial crisis, domestic

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\(^{53}\) Ibid.


\(^{55}\) Ibid.

\(^{56}\) Ibid.
demand of most countries in Asia remains robust, exports continue to expand, and consumer power grows positively. Like China, there is continued enthusiasm in the emerging markets for cars, electronic products and information-technology products. The relatively cheap workforce is one very attractive thing for foreign companies as well. The large Asian market leads many investors to continue to come to Asia. The EU will not be the exception. The growth of Asia is the main stimulation for the re-orientation of EU policy towards Asia and China.

3.3 The Rise of China

During the past two decades, major developments have taken place in Asia. One highlight is the rise of China, one of the very few socialist countries to make a successful transition from a centrally planned economy to a market economy. China is the fastest growing country in East Asia. Because of a rising economic development rate, China is seen as another economic miracle in the early 1990s after the emergence of the ‘four little dragons’ (Hong Kong, Korea, Singapore and Taiwan) in the late 1970s. China has enjoyed a clear acceleration of GDP growth since the economic reform and the open-door policy (see table 1) was adopted in late 1978 to encourage foreign investment. These policies gradually lessened the government’s control of the economy and allowed some aspects of a market economy. “The annual growth rate of China's GDP was 8.5 percent per annum in the early reform period (1979-84). The growth rate accelerated over time and reached nearly 10 percent per annum in the period of 1990-2000”.\(^57\) China’s GDP remained the world’s 10th after the US, Japan, Germany, France, Italy, the Great Britain, Spain, Canada, and Brazil in 1993, and rose to the seventh in the world exceeding Spain, Canada and Brazil in 1998, accounting for 2.5 percent of world’s total and 12.9 percent of developing countries’ total.\(^58\) China has been relatively unscathed from the East Asian currency crisis in 1998. In 2002 China’s GDP increased to the 6th largest in the world. And despite the SARS epidemic, China managed to reach a 9.1 percent growth in 2003.\(^59\)

\(^57\) China’s economy and implicational for U.S. policy.  
http://www.stanford.edu/~ljlau/Presentations/Presentations/020503.pdf

P.83-84

\(^59\) Chinese Economy http://news.creaders.net/headline/newsPool/20A191672.html
In terms of trade, “China’s average annual growth rate of exports has been about 13 percent over the past two decades”.\textsuperscript{60} In 2002 China’s total value of imports and exports reached US$620.8 billion, an increase of US$21.7 billion over 2001. This scale of trade makes China the 6\textsuperscript{th} largest trading country in the world.\textsuperscript{61}

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<tr>
<th>Time Period</th>
<th>Average Annual % Growth</th>
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<tbody>
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<td>1960-1978 (pre-reform)</td>
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<td>1979-1984</td>
<td>8.5</td>
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<td>1990</td>
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<td>2003</td>
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**Sources:** collected from Official Chinese government data reported by the World Bank, and from Chinese statistics bureau.\textsuperscript{62}

China’s growth as a major economic and trading power has impacted China-EU trade relations. It is believed that China’s growing economy is an incentive for the EU’s engagement with China. A series of EU policies towards China adopted in recent years indicate that the EU has recognized the rise of China’s economic growth. In 1995, the EU adopted a Communication on a long-term policy for China-Europe relations that provided a framework for the future development of the EU’s relations with China. In 2001, the EU Strategy paper on *implementation of the 1998 Communication and future steps for a more effective EU policy* stated that the EU needed to re-focus EU policy towards China in regards to the significant development of China, including China’s increasingly

\textsuperscript{60} Yang Fengmin (2001), Chinese Trade Policy of European Union. Huadong Ligong University Press.

\textsuperscript{61} China’s economy and implicational for U.S. policy. [http://www.stanford.edu/~ljlau/Presentations/Presentations/020503.pdf](http://www.stanford.edu/~ljlau/Presentations/Presentations/020503.pdf)

assertive international role and growing political and economic weight.\textsuperscript{63} China is already the world’s sixth largest trader, the second largest recipient of Foreign Direct Investment after the US. Membership in the WTO will give China added impetus in implementing economic and social reform. It will boost confidence, generate domestic and foreign investment, and stimulate economic growth overall as well. The World Bank forecasts that China will “become one of the top three traders in the world by 2020”.\textsuperscript{64}

Thanks to the growth of her trade scale, China’s foreign currency reserves are increasing progressively. “In 1978 China’s foreign currency reserves were only $0.84 billion dollars far behind the foreign currency reserves of Korea ($2.74 billion dollars), Thailand ($1.97 billion dollars) and Philippines (US $1.75 billion) during this period”.\textsuperscript{65} Since 1978, China’s foreign currency income has taken a favorable turn. China’s foreign currency reserves reached $5.98 billion dollars in 1995, staying the world’s fifth after Japan, Taipei, Germany and the US.\textsuperscript{66} At the end of the first quarter of 2003, China’s foreign currency reserves stood at US $31.6 billion, making China the second in the world based on foreign currency reserves.\textsuperscript{67} The increase in the foreign currency reserves provides a firm foundation for resisting financial risks, safeguarding international prestige and keeping economy steady. The rapid development of economic strength has gradually strengthened China's military and political strength, and the influence of China in international affairs has improved as well.

\textbf{3.4 The Integration of the EU}

There have been significant developments in the EU that can and do impact China-EU trade relations, including the on-going integration process and the eastern enlargement.


\textsuperscript{64} EU (1998), \textit{Building a Comprehensive Partnership with China}. http://europa.eu.int/comm/external_relations/china/com_98/index.htm


\textsuperscript{66} \textit{Ibid.}

The EU, the successor body to the EC, currently is a custom union of 15 member nations. France, West Germany, Italy, the Netherlands, Belgium, and Luxembourg set up the EC by signing the Treaty of Rome in 1957 to push the economic integration and the establishment of one big Europe. The United Kingdom, Ireland, and Denmark joined the EU in 1973; Greece joined in 1978; Spain and Portugal joined in 1986; and Austria, Finland, and Sweden became members of the EU in 1995. The major step toward integration was the adoption of a single currency by 11 members of the EU in 1999. The common market, wherein capital, goods and people move freely, is finally established through the implementation of the common monetary policy and common currency. This step has increased the EU’s overall competition and leverage in the global market.

The EU has become a major political and economic force. Its GDP was about $6.7 trillion, with a per capita GDP of $18,000 in 1995.\(^{68}\) Accounting for 40% of international trade (including the trade among EU member states), and 30% of total world stocks of foreign direct investment, the EU is the world’s largest multi-nation trading bloc as well as the world’s prime source of FDI outflows.\(^{69}\) Over the past five years, the EU has been the largest Foreign Direct Investor in China. With a population of about 368 million, the EU is one of the world’s most important markets making it an attractive market for Chinese companies. In addition, in May of 2004 the EU will welcome 10 more new members including Poland, Hungary, the Czech Republic, Slovenia, and Estonia. China’s policy paper states "the new European Union would then cover much of Eastern and Western Europe with an area of four million square kilometers, a population of 450 million and a GDP of over 10 trillion US Dollars".\(^{70}\)

The enlargement of the EU brings opportunity as well as challenge to EU-China trade relations. Opportunities arise from an the enlarged EU bringing benefits in terms of lower tariffs for Chinese exports as the new EU members’ external protection comply with EU Level. It may also bring the risk of trade diversion as analyzed in chapter 4.4.

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\(^{68}\) The European Union. [http://dosfan.lib.uic.edu/ERC/bureaus/eur/releases/950520EU.html](http://dosfan.lib.uic.edu/ERC/bureaus/eur/releases/950520EU.html)

\(^{69}\) EC Delegation in Beijing. [http://www.delchn.cec.eu.int/cn/eu_guide/Trade_Relations_Multilateral.htm](http://www.delchn.cec.eu.int/cn/eu_guide/Trade_Relations_Multilateral.htm)

3.5 Analysis of the Motives

3.5.1 China’s Motives

For China, the reinforcement and development of China-EU trade relations will help diversify China’s foreign trade. China’s foreign trade, especially export, has mostly depended on the US and Japan for a long time. Currently the US is China’s primary trade partner. Recent controversies over trade with the US reminded China of the disadvantages of over-reliance on the US for export. The first disadvantage is that a large amount of Chinese products exported to the US market would cause excessive competition, thus impacting negatively on the price of Chinese export merchandise and the benefit from export trade (See table 2: case study). If Chinese companies reduce the price to acquire the American companies’ order, the Chinese companies are likely to be accused of dumping sanctions and might have other trade restrictions imposed. This creates a trade dilemma for China and Chinese companies.

Table 2: Example 1

<table>
<thead>
<tr>
<th>How much could China gain from her export over dependence on the US?</th>
</tr>
</thead>
<tbody>
<tr>
<td>More and more studies indicate positive prospects for the development of China’s economy. They indicate that China is already a major trading nation, and it will become the second biggest trade power in 2010.\textsuperscript{71} However, what the studies do not specify is how much China gains from her trade. China is a big export country and her export goods have mainly been flowing into the US. What has China gained from her export over dependence on the US? According to the news cited by Xue Yong from the Wall Street Journal, the American company, Wal-Mart, imported 12 billion dollars worth of goods from China, accounting for 8 percent of its total import in 2002. In 2003 Wal-Mart’s import from China rose up to 15 billion dollars\textsuperscript{72}. Apparently, Chinese companies would get a huge benefit from such a trade boom. However, a deeper analysis of this case would give one a less optimistic view. The Wall Street Journal stated that a certain kind of electric appliance supplied by one of the Wal-Mart’s Chinese provider was bargained from $7 dollars 10 years ago to $4 dollars in 2003.\textsuperscript{73} This decrease in price impacted the survival of this Chinese factory. This situation forced the factory to let half of its staff leave, only retaining 1500 staff producing the same amount of products as before. Many workers often worked overtime, sometimes 18 hour a day. However, their monthly salary was less than 300 Yuan.</td>
</tr>
</tbody>
</table>


\textsuperscript{72} China can not be an employee of the world forever. http://www2.bbsland.com/newland/messages/179031.html.

\textsuperscript{73} Ibid.
Renminbi (The name of the Chinese currency. Taking the US dollar for comparison, one US dollar can exchange 8.27 Yuan Renminbi), which is 40 percent lower than the local minimum wage. What makes the Wal-Mart able to bargain down the price so much and why does this Chinese factory not refuse the low price offered by the Wal-Mart? The reason is the current situation in China, which is characterized by an overflow of labor and low domestic purchasing power, forcing the Chinese companies to rely too much upon exportation. Since the US is the biggest and therefore a vital importer of Chinese goods, the US companies have an advantage in business negotiations. The US companies understand this and therefore use this situation to their advantage by making the Chinese companies compete to give the lowest prices.

The enhancement of China-EU trade relations could help China break away from the import restriction on high-tech products from the US as well (as neo-realism suggested ‘balance of power’). The growth of China’s economy is causing some American conservatives’ to panic. They argue that the rise of China will threaten the status of the US in the future. This is the so-called ‘China threat’ theory, viewing China as a threat rather than as a valuable partner. Influenced by such thoughts, the US government has adopted a defensive policy towards China, including the export restriction of certain high-tech products. They believe that China may be able to copy from these high-tech products if they export them to China, thus allowing China to develop technology in these relative field resulting in the loss of the US’s technologic advantage (this thought conforms the assumption of neo-realism in terms of relative gains). For instance, few years ago China ordered a satellite from an American Company and paid the pre-earnest money, 130 million US dollars. The US, fearing that China would probably sharpen her rocket launch ability, did not authorize the satellite export. The Chinese Premier Wen Jiabao, during his visiting to the US in December in 2003, urged the US to lift the various restrictions on exporting to the Chinese market. By comparison, the EU’s technical strength is as advanced as the US. The EU does not like the US imposing export restriction on high-tech products to China. The EU is not only the third largest foreign direct investment source, with investment totaling US $ 4.5 billion, lagging behind the

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74 Ibid.
76 Ibid.
US and Japan, but also the largest technology import source for China.\textsuperscript{77} Moreover, the developments in the areas of institutional reform, enlargement, Economic and Monetary Union, and security and defense policy are inextricably linked to the EU’s ability to become an even more important global partner for China. The EU market is now recognized as a huge and sophisticated market whose recent economic performance continues to be positive and whose future looks promising. An enlarged European Union of 500 million prosperous consumers provides a powerful market for Chinese products and a bigger source of investment. Taking all above-mentioned facts into account, it is safe to conclude that to improve China-EU trade relations are in China’s strategic interest.

\textbf{3.5.2 EU’s Motives}

\textbf{3.5.2.1 The Limitation of EU-US trade}

The EU and the US are not only one another’s largest trading partners but also the largest bilateral trade relationship in the world, resulting in their sheer size and economic strength.\textsuperscript{78} That EU-US economic and trade relations have important economic implications to the EU is beyond question. However, it may be a disadvantage if the EU relies overwhelmingly on the trade with the US. First, the US market has its own limitations for the EU. Both the EU and the US are highly developed industrial countries. They are at broadly similar levels of development and economic structures. For example, both excel at the service sector accounting for roughly 70\% of all output.\textsuperscript{79} Their competitive advantages and the domestic needs are relatively similar leading to a high level of intra-industry trade with the advantage of large-scale production. And it also leads the limited transition space while there is the need of adjusting the production structure. The EU needs different levels of trade products and investment markets to diversify the trade risk. With the liberalization and globalization of economies, the competitive advantage of products moves dynamically among different countries. Some

\textsuperscript{78} EU, bilateral trade relations with USA http://europa.eu.int/comm/trade/issues/bilateral/countries/usa/index_en.htm
\textsuperscript{79} Ibid.
products do not have a competitive advantage in Western counties. For example, the textile and clothes industries are the important and traditional export products for the EU member states. With the adjustment of the world production structure, the competitive advantage of this field has shifted from capital/technology-intensive to labor-intensive, and the economic character of developing country satisfies the demand for this industry advantage. Investing in this field in developing countries is more advantageous than in the US, because the US, like the EU, lacks the competitive advantage in this field.

Regarding the economic benefit, the EU’s transnational companies have a vision of global strategy. They do not just limit their production in the USA. Further, economic similarity is a potential cause of competition between the EU and the US. Many industrial products in the EU and the US’s export are technologically similar and that could result in trade disputes. The increasing trade conflicts between them demonstrate the argument by neo-liberalist that cooperation is based on the degree of complementarities.

The recent economic downturn in the US proves that it is dangerous to continue to rely so heavily on one trading partner for the EU’s well being. From the beginning of the 21st century, the US economy, accounting for one third of the world’s GDP, has begun to decrease. Since the third quarter of 2000 the US economic growth rate has slowed. The ‘9.11’ terrorist attack and expenses for the ‘War in Iraq’ have worsened the US’s economy. “The economic growth of the US in the third quarter of 2001 was -0.4%”\(^8^0\). The depression of the US economy has affected the exports of the EU and has influenced the EU’s economy. The EU cannot rely solely on the US market. To minimize economic risk within the world of interdependence, the EU needs to explore and develop other markets.

3.5.2.2 Market Limitation in Center Eastern European Countries

The EU has focused its efforts on the Center Eastern European Countries (CEECs) in a regional approach. The economic and trade ties between the EU and CEECs have been strengthened. This is because of their geographical adjacency, which is favorable to

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80 China’s economy and implicational for U.S. policy.
http://www.stanford.edu/~jlau/Presentations/Presentations/020503.pdf
developing trade relations. Another reason is that the North Atlantic Treaty Organization (NATO) seeks to incorporate the CEECs into the organization. Most of member states of the EU are members of the NATO; so promoting the trade relations with the CEECs is an import means of expanding the NATO eastward.

The CEECs’ generally economic development level remains a major challenge. The CEECs’ economic weight is insufficient relative to that of the EU. For example, the 12 candidate countries account for 25% of the exiting member’s population but only 4% of their GDP. The investment from the EU flows mostly into the Czech Republic, Poland and Hungary. The trade volume between the EU and Poland, the Czech Republic and Hungary comprises 63% of the EU’s total trade volume with CEECs. The CEECs are basically agriculture countries. With the accession of candidate countries into the EU, “the total farming area will increase by 38% and the number of farms by 75%”. The new comers expect that they could benefit from the accession. Ms Sauvagest points out that the modernization and retraining of workers in the CEECs is a great challenge for the EU. The CEECs are in the process of transitioning, but face difficulties due to the economic depression in their countries. So far, only a few of the countries, such as Poland, Hungary, have relatively good economies. The marketplace of the CEECs has not met the expectation of the EU. The CEECs have not become the new energetic market, but instead have brought a financial burden to the EU. The trade between the EU and the candidate countries translates to only 3.5% of the EU’s foreign trade. Poland’s former foreign affairs minister Bronislaw Geremek deemed that “the economies of eastern and western Europe are not complementary”. The limited growth potential of the EU’s internal market, opening and exploring export markets is the only method of increasing EU production. Moreover, the EU faces competition from the US and Japan, who understand the importance of capturing economic power (as neo-realism claimed)

82 Ibid.
83 Ibid.
84 Ibid.
85 Ibid.
86 Ibid.
and also want to capture the market shares of the CEECs. The EU must take other competitive measures besides enhancing its presence in the CEECs’ market.

3.5.2.3 The Importance of Asia and China

The remarkable growth in Asia is an undisputed fact. Thanks to its size and the scale of its economic growth, Asia has become an increasingly important force in the global economy. Asia’s growing economic weight makes it demand a greater role in world affairs. Asia is gaining a stronger influence in the world balance of economic power. There are currently five great economies, the US, the EU, Japan, China (potential a great economy) and Russia. The driving force in the world economy, at the beginning, was Western Europe. The US replaced the Western Europe in the end of the 19th century, becoming the center of the world economy. At the end of 20th century Asia, especially eastern Asia has become the primary engine of world economic growth. 87 By the year 2000, the World Bank forecasts “the growth in the global economy will come from East and Southeast Asia alone.” 88 A recent major study on long-term development trade has reckoned that by 2050 the center of gravity in the world economy will be the Asian Pacific Region. 89 Faced with the vigorous development in Asia both politically and economically, every country in the world seeks to the accession of Asian market. Could the EU be the exception? All these facts constitute the reconsidering by EU of Asia and China as trading partners.

The EU policy makers see the enormous economic opportunities in Asia. Form a neo-realistic perspective, one country’s gain is another’s loss. The EU believes that if they do not take these economic opportunities, then their competitors will. In the today’s global economy, the lose of any potential market has negative impacts on the capacity to compete. The European Union’s performance in economic and trade relations lagged behind their US and Japanese counterparts in the early years of the growth of the dynamic Asian economies. The EU doubted the future of Asia’s development. Compared

with the US and Japan, the EU’s presence in Asia is relatively weak. Furthermore, the EU’s presence in Asia had been reduced while both the US and Japan promoted relations with Asia. ‘The EU’s total exports to Asia decreased from 25% in 1970 to 15% in 1995. Between 1986 to 1995, the EU only accounted for 10% of Asia’s total foreign direct investment.’\textsuperscript{90} At that time, the EU realized the importance of Asia, and also realized the dangers of the EU’s presence in Asia lagging its competitors. In the last decade economic and trade issues have remained one of the top priorities of EU’s policy for Asia. The issuing of the EU political paper on Towards a New Asia Strategy in 1994 is proof of the change in attitude. How can the EU gain the Asian market as the US and Japan have been involved in promoting trade and economic relations with Asia earlier than the EU? And the US and Japan are strategic partners, so that the question for the EU is how to compete with the US and Japan for the Asian market. The rise of China provides the EU with an opportunity to improve its situation in Asia. China, a growing economic and political power, has significant influence on Asian affairs. Since China has become a member of the Asia Pacific Economic Cooperation (APEC), and especially since the former Chinese President Jiang Zemin attended the unofficial meeting of APEC in Seattle, China’s role and influence in APEC has caught the world’s attention.\textsuperscript{91} China is seen as the key actor in the Asian region. The EU will be able to balance the US-Japan relation if it builds close relations with China. From this point, China forms the core of the EU’s regional policy towards Asia. Thus, having a close economic relation with China is one of the EU’s global and long-term objectives, which is consistent with the EU’s regional strategy.

The above analysis stresses the importance of China for the EU from a regionally strategic concern. I am now going to discuss what China, as an individual country, can offer the EU.

The EU’s main focus in present and future policy with China is related to economic matters. At the end of 1980s and the beginning of 1990s, the EU countries’ economy was

\textsuperscript{90} Yang Fengmin (2001), Chinese Trade Policy of European Union. Huadong Ligong University Press. P.77
\textsuperscript{91} Ibid.
depressed, marked by low growth rate, low productivity and the high unemployment. This caused social problem, such as the outbreak of strike demonstrations in France and Germany. The EU’s economy used to depend on its inner market and other western countries. During recent years, demand and supply from these markets has almost reached saturation. The EU needs to explore new markets to alleviate its internal problems. The rise of China offered the EU an opportunity. China is already the world’s seventh largest trader, the second largest recipient of Foreign Direct Investment. And her purchasing power is “on a par with Japan just behind that of the US”.  

The Asian Development Bank forecasts that China will be the largest trading economy by about 2010, making China an unprecedented opportunity for others. China has become the hot market in the world because of its enormous market for import, its high growth rates, and its new WTO membership. China needs advanced technology, equipment and services to upgrade its consumption structure and infrastructures. The constant development and the enormous market potential of China’s economy make her attractive to the EU, especially when the EU faces economic difficulty. The China’s strong needs for goods (especially the goods of telecommunications, informational society and energy sectors) and capital provide the EU an unprecedented opportunity. That the EU develops its trade relations with China is an inevitable consequence. Not only can the EU gain materially economic benefits from its close trade relations with China, but the EU can gain political advantages as well since trade relations is the starting point for developing bilateral relations. China, as a UN Security Council member and a growing economic and political power, has significant influence on global issues, such as arms proliferation, terrorism, environmental degradation and so on. Through further engagements with China, the EU will be better able to maintain its interests in Asia and elsewhere. In a word, it is in the EU’s interests, both economic and political, to strength its trade relations with China.

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93 http://www.adbi.org/prc2002/papers/33
3.6 Analysis of Total Trading Volume

China-EU trade relations have developed significantly while the economic changes were taking place in both China and the EU. Their development process can be roughly divided into three phases: the initial phase (1949-1974), the legalization phase (1975-1989) and the promotion phase (1991-present).

At the initial phase a number of EU member states, like the Italy, Belgium, Germany and Luxembourg, established diplomatic relationships with China during the early 1970s. The trade during this phase was based only on a China-EU member state level. The second development stage is the legalization phase. At this phase bilateral legal mechanism was built on the China-EU level. There were three major legal developments during this period regulating the China-EU trade relations. The first legal development was the establishment of China-EU diplomatic relationship in 1975. The second was the adoption of the China-EC Trade Agreement in 1978, which was the basis for developing China-EU trade relations at the EU level. The third legal development was the update of China-EC Trade Agreement and implementing the China-EC Economic Co-operation Agreement in 1985, which enlarged the cooperation between China and the EU.

All the above-mentioned legal developments provided both sides with a legal basis for their trade relation. The promotion phase has been in effect since 1991. China-EU bilateral trade relations have entered a new era resulting in both sides seeking to develop their relations constructively and consider their economic relations strategically.

Regarding the total trade volume, China-EU trade can be divided into three distinct periods. During the first period, which ended in 1985, the total amount of import and export lingered under 10 billion US dollars. From 1985 to 1992, the trade amount gradually increased and exceeded 10 billion US dollars. After 1993, the pace accelerated. The total trade in the period between 1993 and 2003 increased dramatically.

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95 Ibid.
96 Ibid.
97 Ibid.
Table 3: China’s trade with the EU: 1975-2003

(Unit: USD billions)

<table>
<thead>
<tr>
<th>Year</th>
<th>China’s export</th>
<th>China’s import</th>
<th>Total trade</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>0.809</td>
<td>1.590</td>
<td>2.399</td>
</tr>
<tr>
<td>1976</td>
<td>0.850</td>
<td>1.661</td>
<td>2.511</td>
</tr>
<tr>
<td>1977</td>
<td>0.880</td>
<td>1.268</td>
<td>2.148</td>
</tr>
<tr>
<td>1978</td>
<td>1.199</td>
<td>2.085</td>
<td>3.284</td>
</tr>
<tr>
<td>1979</td>
<td>1.723</td>
<td>3.341</td>
<td>5.064</td>
</tr>
<tr>
<td>1980</td>
<td>2.300</td>
<td>2.671</td>
<td>4.971</td>
</tr>
<tr>
<td>1981</td>
<td>2.495</td>
<td>2.760</td>
<td>5.255</td>
</tr>
<tr>
<td>1982</td>
<td>2.136</td>
<td>2.484</td>
<td>4.620</td>
</tr>
<tr>
<td>1983</td>
<td>2.219</td>
<td>3.476</td>
<td>5.695</td>
</tr>
<tr>
<td>1984</td>
<td>2.354</td>
<td>3.528</td>
<td>5.882</td>
</tr>
<tr>
<td>1985</td>
<td>2.254</td>
<td>6.107</td>
<td>8.361</td>
</tr>
<tr>
<td>1986</td>
<td>3.993</td>
<td>7.658</td>
<td>11.651</td>
</tr>
<tr>
<td>1987</td>
<td>3.885</td>
<td>7.265</td>
<td>11.15</td>
</tr>
<tr>
<td>1988</td>
<td>4.721</td>
<td>8.15</td>
<td>12.871</td>
</tr>
<tr>
<td>1989</td>
<td>8.76</td>
<td>14.75</td>
<td>23.510</td>
</tr>
<tr>
<td>1990</td>
<td>9.32</td>
<td>12.84</td>
<td>22.160</td>
</tr>
<tr>
<td>1991</td>
<td>5.37</td>
<td>6.24</td>
<td>11.61</td>
</tr>
<tr>
<td>1993</td>
<td>11.693</td>
<td>11.412</td>
<td>26.05</td>
</tr>
<tr>
<td>1995</td>
<td>19.09</td>
<td>21.25</td>
<td>40.34</td>
</tr>
<tr>
<td>1997</td>
<td>23.811</td>
<td>19.192</td>
<td>43.004</td>
</tr>
<tr>
<td>1999</td>
<td>30.211</td>
<td>25.465</td>
<td>55.676</td>
</tr>
<tr>
<td>2000</td>
<td>38.193</td>
<td>30.845</td>
<td>69.038</td>
</tr>
<tr>
<td>2001</td>
<td>40.904</td>
<td>35.723</td>
<td>76.627</td>
</tr>
<tr>
<td>2002</td>
<td>48.212</td>
<td>38.543</td>
<td>86.755</td>
</tr>
<tr>
<td>2003</td>
<td>72.155</td>
<td>53.062</td>
<td>125.217</td>
</tr>
</tbody>
</table>

Source: collected from Chinese statistics bureau and China’s Customs statistics

In terms of import and export, the bilateral trade has experienced three stages from 1975 to 1996. Before 1984, China’s trade with the EU was balanced, and the gap of import and export was narrow. After 1984, the growth of trade achieved an unfavorable balance, reaching a peak in deficit trading of $6 billion in 1989. The trade deficit with the EU remained roughly $2 billion during 1990 and 1995, and reached zero in 1996. The trade deficit changed in 1997 with a trade surplus around $4.7 billion, and the tendency toward a trade surplus remains as a concern for the EU.

According to the data from table 3, I formed an EU-China trade tendency chart (Graph 2) below. From this graph one notices there are three turning points from 1975 to 2003. The growth of China-EU trade in the period between 1975 and 1988 is flat. The primary reason for this is that the EU was involved in its internal affairs, such as the negotiations...
on EMU and the other preparations for the Maastricht Treaty in 1992. At the same time, the recovery from the impact of the Chinese Culture Revolution, which started in 1966 and ended in 1976, causing great damage to the Chinese economy, absorbed much of the energy of China. As a result the development of China-EU trade was sluggish during this period. The year 1986 shows the first peak in trading. By comparing with the figure in 1985, the growth rate was 39%. The trade growth in 1986 can be attributed to the enlargement of the EU. Trade between China and the EU was suspended in 1989. This was caused by the outbreak of the Tian Anmeng issue, which led the EU to freeze relations with China and adopt a series of sanctions on China. As a result, China-EU trade decline steeply from 1990 and reached the lowest point in 1991. The EU resumed relationships with China in 1992 and bilateral trade dollars increased. In 1995, because of the third enlargement of the EU, the total trade volume reached another peak. The continuous increase since 1996 is reflected in the readjustments in policies from the EU side, notably the adoptions of EU policy paper on ‘A Long-term Policy for China-Europe Relations’ in 1995 and on ‘Building a Comprehensive Partnership with China’ in 1998.

Graph 2: EU-China trade tendency

![EU-China trade tendency graph](image)
From the data and analysis stated above, it is clear that the trend-line of China-EU trade is upwards. With the upcoming of the EU’s fifth enlargement and China’s accession into the WTO that will lead further reforms in economics and politics, it is reasonable to forecast that the prospect of China-EU trade is positive.
CHAPTER 4: THE CURRENT ISSUES

4.1 Introduction

This paper documents the current trade development between China and the EU. In this chapter the main constraints to trade will be discussed.

China-EU economic and trade ties have expanded substantially over the past two decades. The total trade volume has grown more than 40-fold in 2002 since 1977 (see table 3). As bilateral and economic relations grow, friction is inevitably unavoidable. China-EU trade relations face a considerable number of challenges and uncertainty. The first challenge is the upcoming EU enlargement. Due to geographic proximity and the similarity of culture and ideology, 60 percent of the EU trade takes place within the EU.\(^98\) The EU market characterizes exclusiveness, saturation and limitation. There is the possibility that closer integration and enlargement of the EU could make it more self-contained and inward looking. Intra-EU trade could increase, while trade with the rest of the world could diminish. One more concern for China is that the enlarged EU would suck in capital from China to the EU. The impact of the EU enlargement on China-EU trade relations will be discussed in chapter 4.4.

The second challenge in China-EU trade originates from the weakness of China in production capacity, management and technical knowledge. In order to seize a share of the EU market, China needs to improve the quality of her production and enhance the quality of service to meet the needs of the EU market. China must heed the EU regulations and criterion on import goods, such as security and environmental requirements in order for Chinese goods to enter the EU market.

Considering the difference in social system, ideology, culture, and particularly because their bilateral trade relationship becomes more important and ever more integrated, it is

unavoidable resulting a growing list of trade conflicts, ranging from traditional tariff and non-tariff barriers. Long-standing disputes are trade balance, anti-dumping, textile quotas, and market access. These trade disputes, which threaten the further development of China-EU trade relationships, need to be managed. In this chapter anti-dumping, which is one of the primary trade clashes between China and the EU, will be analyzed closely.

4.2 Trade Balance and China’s WTO Membership

China-EU trade relations have been strained by a number of issues. For example, the EU policymakers have expressed concern over the bilateral trade balance.

The issue of bilateral trade balance can be traced to when the official trade relationship was established between China and the EU. In the period from 1975-1996 periods, the EU enjoyed a trade surplus with China. From 1997 on the China-EU trade is marked by a widening EU deficit with China. The bilateral trade balance has aroused attention and caused problems for the development of a China-EU trade relationship, especially the size of the EU deficit that has been largely exaggerated by the EU side. In 1997, the EU’s trade deficit with China was $4.7 billion, and has been increasing, reaching around $19 billion in 2003 (see table 3). The EU trade deficit with China, which is likely to grow, worries the EU.

Many analysts argue that the EU’s growing trade deficit mainly reflects the effect of market access obstacles in China. Market access obstacles include high tariffs, non-tariff barriers, non-transparent trade rules and regulations and investment restrictions.

- **High tariffs.** The average Chinese tariff rate is currently 17%. And tariffs on autos and various agricultural products can be to 100% or more.\(^{99}\)
- **Non-tariff barriers** include quotas, import licenses, registration and certification requirement, which are used to control the level of certain imports into China.\(^{100}\)

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\(^{100}\) *Ibid.*
• **Non-transparent trade rules and regulations.** “China's trade laws and regulations are often secretly formulated, unpublished, unevenly enforced, and may vary across provinces”.\(^\text{101}\) It makes it difficult for exporters to determine what rules and regulations apply to their products. Further, when foreign firms want to appeal new trade rules and regulations they find it difficult to come in contact with government trade rule-making agencies. There is a lack of consistent trade laws.

• **Investment restrictions.** Control of some sectors such as banking, insurance and telecommunications are in the hands of the Chinese government. In these sectors foreign investment is highly restricted.

To improve market access and investment environment in China would likely lead to relax the conflicts of China-EU trade relations. China’s entry into the WTO on December 11, 2001 has created a favorable turn in trade relations with the EU. The EU policy-makers believe that China’s WTO membership will “iron out such barriers and help create an open Chinese economy that benefits EU’s interests”.\(^\text{102}\) With this in mind, the EU has been a strong backer of China's entry into the General Agreement on Tariffs and Trade (GATT), and supports China's entry to the World Trade Organization (WTO). The EU is attempting through these international agreements to secure similar access and operating conditions for European businessmen in the China’s market as the current conditions enjoyed by Chinese businessmen in the European market.

In the bilateral agreement between China and the EU on China’s entry into the WTO, China is committed to:\(^\text{103}\):

- reducing import tariffs on over 150 European exports, including machinery, textiles, clothing, glass, leather goods, and cosmetics;
- cutting tariffs and removing non-tariff barriers for key EU agricultural products, such as rape-seed oil, dairy products, pasta, wine and olives;

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\(^{101}\) *Ibid.*


\(^{103}\) China-EU agreement on WTO accession. http://www.chinalegalchange.com/Archives/arch0010.html
• reducing restrictions on auto trade. Auto quotas would be eliminated by 2005;
• opening gradually its service sectors such as banking, insurance, and telecommunications after China’s accession to WTO.

It is obvious that China’s accession into the WTO will improve access conditions for EU firms to China’s market by the sharp reduction in the import tariffs and other non-tariff barriers. Benefiting from lower tariffs, the EU hopes that China’s accession into the WTO will enable the Chinese economy to maintain a relatively high growth rate. In future decades, the huge potential market in China will turn into a market reality, creating great business opportunities for the EU. For China, its WTO membership allows greater access to EU’s domestic market, helps with fairer trade indiscrimination treatment, attracts more foreign investment and technological know-how, and accelerates its own process of economic reform and development. The restrictions on China’s farming and sideline products will be lifted as well.

China’s WTO entry gives new impetus to China-EU trade growth and development. It provides effective institutional and legal guarantees for bilateral trade. China’s WTO membership also brings potential obstacles for bilateral trade. For example, according to the WTO exception principle, its members are allowed to take certain protective measures to protect domestic industries from outside competition. The EU’s anti-dumping mechanism against China will last for another 15 years. Furthermore, China’s WTO entry allows better access to the EU market, which will probably lead the EU to become more active in using anti-dumping mechanism against China to protect its inter-market. This may result in worsening China-EU trade relations.

### 4.3 Anti-dumping Policy

Anti-dumping is emerging as a major source of trade disputes between China and the EU. Anti-dumping practice is an extremely problematic area for Chinese exporters.

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104 Dumping occurs when goods are exported at a price less their normal value, generally meaning they are exported for less than they are sold in the domestic market or third-country markets, or at less than production cost.
In recent years there has been an increase of EU anti-dumping actions against China. The EU initiated the first anti-dumping case against China, involving saccharin and its salts, in 1979 when China had just started economic reforms and the open door policy towards the West.\textsuperscript{105} “Between 1979 and 2000, the EU initiated or reviewed nearly 90 anti-dumping proceedings against China, making China the most accused country of EU antidumping charges” (see table 4).\textsuperscript{106} “In 2000 the antidumping charges against China reached a peak of around 20\% of the EU’s total annual antidumping proceedings”.\textsuperscript{107} Table 4 shows the sector distribution of EU anti-dumping cases against Chinese products from 1979 to 2000. It is not difficult to notice that there has been a shift of EU anti-dumping initiations from chemical, mineral/ores and machinery sectors in the early 1980s to electronics and mechanical goods in the later 1990s.

\begin{table}[h]
\centering
\begin{tabular}{|c|c|c|c|c|c|c|}
\hline
Year & Chemical & Textile & Mechanical & Electronics & Iron and steel & Ores & Agricultural & Total \\
\hline
1979 & 1 & 0 & 1 & 0 & 0 & 0 & 0 & 2 \\
1980 & 1 & 0 & 0 & 0 & 0 & 0 & 0 & 1 \\
1981 & 2 & 0 & 0 & 0 & 0 & 0 & 0 & 2 \\
1982 & 1 & 0 & 0 & 0 & 2 & 1 & 4 &  \\
1983 & 2 & 0 & 0 & 0 & 0 & 0 & 0 & 2 \\
1984 & 1 & 0 & 1 & 0 & 0 & 0 & 0 & 2 \\
1985 & 0 & 0 & 1 & 0 & 0 & 0 & 0 & 1 \\
1986 & 1 & 0 & 1 & 0 & 0 & 0 & 0 & 2 \\
1987 & 0 & 0 & 0 & 0 & 0 & 0 & 0 & 0 \\
1988 & 4 & 0 & 1 & 0 & 2 & 0 & 7 &  \\
1989 & 0 & 3 & 0 & 0 & 2 & 0 & 5 &  \\
1990 & 2 & 1 & 2 & 1 & 0 & 1 & 0 & 6 \\
1991 & 0 & 0 & 1 & 1 & 0 & 2 & 0 & 4 \\
1992 & 3 & 0 & 2 & 1 & 0 & 2 & 0 & 8 \\
1993 & 2 & 0 & 0 & 1 & 0 & 1 & 0 & 4 \\
1994 & 3 & 1 & 0 & 0 & 1 & 0 & 5 &  \\
1995 & 2 & 2 & 1 & 0 & 0 & 0 & 0 & 5 \\
1996 & 1 & 4 & 0 & 0 & 1 & 0 & 6 &  \\
1997 & 2 & 1 & 0 & 2 & 0 & 0 & 0 & 5 \\
1998 & 0 & 0 & 0 & 0 & 1 & 0 & 1 &  \\
1999 & 3 & 0 & 4 & 3 & 2 & 0 & 12 &  \\
2000 & 3 & 0 & 0 & 1 & 0 & 2 & 0 & 6 &  \\
Total & 34 & 12 & 14 & 11 & 5 & 3 & 1 & 90 & \\
\hline
\end{tabular}
\caption{EU anti-dumping cases against Chinese products across year and sectors (1979-2000)}
\end{table}

Source: cited from Xiang Liu and Hylke Vanderbussche (2002)\textsuperscript{108}


\textsuperscript{106} Ibid.

\textsuperscript{107} Ibid.

\textsuperscript{108} Ibid.
Some conclusions can be derived from the EU anti-dumping cases against Chinese products, which seem to have affected the vulnerability of Chinese products to EU anti-dumping charges. These are:\footnote{Ibid.} (i) the non-market economy treatment of China; (ii) the strength of product market competition between Chinese and European companies; (iii) the trade deficit that the EU has been running with China; (iv) the ownership structure of Chinese exporters and the very concentrated nature of the market structure of EU producers involved in formulating complaints against Chinese imports. For instance (see Table 5: case study), companies involved in the case of Chinese ‘electronics balance’ products are state-owned enterprises. Generally speaking, state-owned enterprises in China operate more or less under softer budget constraints than private firms because they are either subsidized by the state or enjoy tax or credit advantages. This may possibly lead to low prices that can consequently result in anti-dumping protection. The case implies the fact that state ownership of the Chinese defendants positively affects the probability of EU anti-dumping protection. However, with the further reform of Chinese economy especially with the privatization of state-owned enterprises, the application ‘non-market economy treatment’ towards Chinese export companies seem an arbitrary methodology. By defining China as a non-market economy, the EU anti-dumping polices do not acknowledge China’s domestic costs of production. The cost of production is determined using a third ‘surrogate’ country to calculate the ‘normal value’ of Chinese exports. Using non-market criteria allows the complainant to ignore local Chinese prices. Moreover, the problem with anti-dumping disputes for Chinese firms is the expense to defend itself once it is accused of dumping. It is not difficult to launch an anti-dumping action in the EU. All that is needed for domestic producers is to petition the EU to start an investigation. The target of the investigation must spend perhaps more than US $100,000 to defend itself.\footnote{Yang Fengmin (2001), Chinese Trade Policy of European Union. Huadong Ligong University Press.} These costs are a burden even for a medium-sized Chinese company.

The EU has been implementing a relatively severe anti-dumping policy towards China in recent years. Although the EU has agreed to remove China’s ‘non-market economy’ label, China still cannot be granted market economy treatment. Currently only
a few Chinese export companies have gained ‘market economy treatment’. In 2000 the number of antidumping proceedings against China initiated by the EU reached a historic peak. This issue of dumping and anti-dumping policy has become major obstacle in China-EU trade relations. After China joins the WTO, China will have easier access to the EU market, which will probably influence the EU to become more active in the use of anti-dumping proceedings against China in an attempt to protect and promote domestic industries. These possible anti-dumping actions worry China.

Although the anti-dumping measures are enforced to maintain fair trade conditions and have to be used under the WTO’s approve, in recent years the concepts have strayed from the original intention and have become part of trade protectionism using by developed countries against the developing countries. This worries developing countries. The misapplication of anti-dumping policy will undermine the development of China-EU trade relations. As a WTO member China will be able to resort to the WTO dispute settlement mechanism to resolve disputes with its trading partners in relation to anti-dumping measures. In retaliation China began to use the anti-dumping measures on the EU’s products. The EU should recognize if there is no clearly defined evidence, there would be a risk in using anti-dumping measures. There is reciprocity in the market and the resources between EU and China, therefore the anti-dumping measures should be used properly so that a healthy relationship can develop between these two giants.

Table 5: Example 2

<table>
<thead>
<tr>
<th>Anti-dumping case-Chinese ‘electron balance’ products.111</th>
</tr>
</thead>
<tbody>
<tr>
<td>On July 30, 1999, the major producers of ‘electron balance’ in the European Commission appealed the anti-dumping investigation for the electronic balance imported from China. On September 16, 1999, the EC decided to investigate the anti-dumping case. In this case, three Chinese companies applied for the status of market economy. One of them was turned down due to a missed deadline for submitting the related information to the European Commission. The other two enterprises were investigated and neither was given the status of market economy because they didn’t meet the requirement of the EU anti-dumping law. However, all three Chinese companies applied for the status of individual case and were approved.</td>
</tr>
</tbody>
</table>

The final judge of this case is that the products imported from the related Chinese companies influenced essentially the industry in the Community. The anti-dumping duty was imposed. Chinese companies obtained the treatment of ‘individual case’.


49
(1) Determination of dumping
   (i) Reference country choosing.
   In the case that no Chinese company satisfies the market economy position, according to EU’s anti-dumping article 2(7), the export prices of Chinese export vendors must be compared with the standard prices of one of market economy countries to calculate dumping extents. In this case, both defendant and EU propose Indonesia as the reference country. No one opposes this. An Indonesia company cooperated and submitted the information.
   (ii) The comparison between normal value and export price.
   The comparison is made on the basis of the out-of-plant price. To ensure fairness, according to EU’s anti-dumping article 2(10), the differences of the factors that bring effects to the prices and the price comparability should be considered. For example, the differences on transportation, insurance, loading and unloading, shipping and ancillary costs, and loan, salary, import tax and duty, after-sale services (warranty/guaranty).

(2) Determination of injury.
According to EU’s anti-dumping article 3(5), the EU committee evaluates the effects suffered by EU industry, including all economic factors and indices related to industry conditions.
   (i) Produce, production capability utilization rate and storage. The production of all electronic balances during the investigation period increased 22%. Compared with this, the production of low-level products during the investigation period only increased 5%. Production ‘capability utilization rate’ increased from 55% to 65% during the investigation period. The level of storage could not be considered having great effects to EU industry situation because EU produces following the orders, there is almost no storage.
   (ii) Sales quantity. Sales quantity of all electronic balances produced by EU industry in the EU market increased 29% during the investigation period; the sales quantity of low level electronic balances increased only 10%.
   (iii) Sales. Sales of all electronic balances produced by the EU industry in the EU market increased 27% during the investigation period; the sales quantity of low level electronic balances increased only 11%.
   (iv) Market share. Market share of all electronic balances produced by the EU industry in the EU market decreased from 26.1% in 1995 to 24.9% during the investigation period. The market share of low level electronic balances decreased from 21.8% in 1995 to 17.1%. Thus, EU industry could not obtain benefit from the market growth.
   (v) Sales price. During the investigation period, the sales average prices of all levels of electronic balances to non-related customers decreased. Though there is one export producer pointed out, during the investigation period, the average price of all electronic balances increased slightly, the EU industry was not injured. But, this superficial increase is thoroughly from the change of mixed products (namely the changes of the sales number of each level of products from 1995 to the investigation period). Thus, the opinion was not adopted.
   (vi) Profit. Electronic balance revenue increased from a low percentage to about 10% of the investigation period. But, low-level products increased from low profits in 1995 to the actual loss (about 20%) in the investigation period.
   (vii) Productivity, labor hours and salary. During the investigation period, EU labor hours decreased 11% while individual productivity increased 40%. Considering the importance of other business share in the whole company business, the detail analysis to salary was not conducted.

As a summary of the above analysis, EU committee reached the following conclusions: During the investigation, the average price of 3 categories of products of the EU industry decreased, market shares reduced. The investigation to the low-level electronic balances (sales quantity, average price, production, market share and profit rate) shows, the total trend of this product essentially badly changed. Thus, the EU industry was considered to have suffered injury.

(3) Determination of causal relationship
During the investigation, the Commission evaluates the influence of the dumping on the European industry.
   (i) The influence of the dumping products. The consumption increases 35 % but the sales of European industry increased only 29%, and the amount of import from China increased 123%. The market share of the Community industry decreased 4.6%. The market share of Chinese goods has increased from 9.2 to 15.1. The sales price in the EU also drop. All of these factors had a negative effect on the EU. This analysis shows that the decrease of the financial and economic index is related to the growth of imported goods from Chinese company.
   (ii) The effect of EU internal competition. Export producers put forward, the internal competition of EU
electronic balances market caused by the structural change of EU retail industry has effect on price decrease. The EU committee believed lower price competition, on the one hand gives big market share to the dumping imported products of the involved country, on the other hand, EU industry loses the corresponding market share and thus lowers the sales price. Considering the cause-effect relationship of these 2 parts, the imported products dumped by the involved Chinese companies brought substantial damages to EU industry.

(4) Community interest test
The benefit of the EU industry. If no measures are taken to the harmful dumping, the benefits of EU industry on market shares, profit rate and labor hours will be injured. The dumped imported products bring direct negative impact over, and the EU could not accept such impacts on its lower products.

During the investigation period, large scale of re-organization and combination has happened to EU industry. This is the continuity of the various combinations and acquisition emerged in 1990, in order to ensure the survival of the electronic balance production in EU and thus on the whole protected this patent. If no effective actions were taken, there would be inevitably impacts to the industry vendors and the corresponding businesses in the EU internal industry (profit rate and labor hours lowered). This is because the electronic balance technology and all other related series of products, if the harmful dumping were allowed, the relevant labor hours would be affected. The EU committee believed the dumping of products from the involved countries brought substantial injury to EU industry. EU has expended efforts to keep its competitive position. This injury was covered by the short-term benefits brought by the introduction of Euro. If no effective measures are taken, along with the disappearance of the Euro effects, EU industry might be further injured and the production of low-level electronic balances might be stopped, and thus the variety of EU industry might be threatened.

(5) Judgment conclusion
The EU committee adopted the representative production costs of 2 basic low level products of the EU industry, plus 10% profit.

4.4 The Negative Impact of EU Enlargement

Economic integration between the EU and the CEECs has increased dramatically since the 90’s. The enlargement of the EU on May 1, 2004 with ten new members, eight of which from central and Eastern Europe, will impact profoundly on China-EU trade relations.

One advantage of the EU enlargement is that Chinese companies will have an opportunity to access a larger EU market of some 450 million people. Chinese companies may benefit from a single set of trade rules, a single tariff, and a single set of administrative procedures that will apply across the enlarged Union. Inevitably, the occurrence of every event has its advantages as well as disadvantages. Some negative impacts with the upcoming EU enlargement are discussed in the following aspects.
The risk of trade diversion. Successive enlargement of the EU is encouraging many European firms to be more self-contained and inward looking. Intra-EU trade will increase, especially since the most of the EU’s newcomers are from central and Eastern Europe. In the terms of economic development level and industrial structure, these new EU members are similar to China. This will result in competition between China and the EU’s new members in terms of trade. As a practical example: China is a relatively large source of many EU imports, especially labor-intensive products. Some labor-intensive and resource-intensive products that the EU currently trades with China will more likely be traded with Eastern European countries within the EU rather than with China. This can cause a trade diversion.

The risk of aid diversion. With the planned EU eastern enlargement, the EU budget directs that the pre-accession aid towards CEECs would reach €18.92 billion during the years from 2000 to 2006. This budget aggravates the EU financial burden and the distribution of the EU aid. It may lead to the decrease of the aid from the EU towards other developing countries including China.

The risk of investment diversion. The fifth EU enlargement causes China to fear that the EU’s upcoming inclusion of Poland, Hungary, the Czech Republic, Slovakia, Estonia, Latvia, Lithuania, Malta, Slovenia and Cyprus will almost certainly force Europe’s richest countries to focus on their new partners in Central and Eastern Europe, at the expense of China. While the EU has been the fourth largest foreign direct investor in China, there are several reasons why this role may be weakened after May 1, 2004 as following.

- The EU will try to lift the newcomers from poverty. The average GDP per capital of the new members accounts only for 38 percent of the EU average, which means that it may take decades of FDI or other measures to help them catch up to current European standards.

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113 Obstacles of eastern enlargement. http://www.cap.uni-muenchen.de/download/2000/obstacles.doc
• The ten new EU members make up a large potential market of nearly 100 million consumers. After the accession, these new EU members, according to the EU law, will join the EU single market where capital can flow freely aiding the EU investor. Further, in the single market all commerce operations follow one common policy. The EU investors understand this policy better, which make them feel more secure. For them, Chinese law is not transparent enough and is characterized by unclear legislation increasing the risk for investing and doing business in China. Taking into effect all of the above-mentioned factors, the EU enlargement will encourage many EU firms to look to investment opportunities closer to home.

• Low labor force costs, relatively qualified workforce, and geographic proximity with the current EU members are advantages for the EU newcomers. The newcomers are in the process of privatization and modernization. Their accession, undoubtedly, will facilitate the EU investors. The convenient investment environment of the newcomers may be are at the cost of China. There is a possibility that FDI to the CEECs may displace FDI going to China.

4.5 The Issue of Human Right

After the end of the cold war, a commitment to universally recognized western democracy and human rights lies at the heart of the EU’s foreign policy. The EU believes that these principles are inextricably adhered to a country’s economic development and prosperity, and political stability, so that full respect for these principles is set as the requirement within the frameworks of the EU’s bilateral relations with other countries.114

Towards the relations with China, the EU expressed concerns of China being able to transition to an open society based on the rule of law and the respect for human rights. The EU’s policy paper, ‘a Long Term Policy for China Europe Relations’ issued in 1995, states that “the importance attached to human rights has been a consistent feature of the

EU’s policy towards China”.115 The European Commission also proposed that the EU’s aid towards developing countries should be considered in conjunction with the progress in human rights and democracy of these countries. The EU will only aid the countries in which progress has been achieved on these issues. It is therefore obvious that human rights remain a sensitive political issue in China-EU trade relations.

In the process of analyzing the relations between the total trade volume and non-economic factors, one notices that human rights issues, politically, continue to dominate China-EU trade relations. According to table 6, China-EU trade can be divided into three stages. The first stage is the period from 1975 to 1988. During this period, China-EU trade had grown gradually without the interference of the human rights issue. The total trade in the period between 1975 and 1988 increased more than five times. The human rights issue influenced the second stage from 1989 to 1991. The steady development of bilateral trade relations was interrupted by the 1989 Tiananmen Square event, when China was accused of violating human rights. The EU enacted a number of sanctions towards China, for example suspending all military contacts and arms sales and freezing all government-guaranteed loans, causing the trade between the two sides to drop rapidly. The total trade decreased from $23.5 billion in 1989 to $22.1 billion in 1990 (see table 6). This tendency continued until 1991 when the total trade fell to $11.6 billion. In this period the total trade volume declined $11.9 billion. In the third stage since 1991, with the normalization of relations and with the improvement of human right condition, the effect from the human rights issue has been reduced and bilateral trade has been rapidly escalating. The big step in 1994 was bilateral cooperation and the re-opening of political dialogue. This has paved the way for a surge in bilateral trade. In 1997, the bilateral trade entered into a new stage with the total trade exceeding $43 billion. It is also the year of resumption of dialogue between China and EU on human rights that has been interrupted in the spring 1996.

If this observation is accurate, as I believe it is, it might be reasonable to conclude that the influence of human rights issue on bilateral trade is direct. When there is no deviation on human rights issues between China and the EU, the bilateral total trade volume increases. Contrarily, the trade volume decreases.

Table 6: The comparison of the total trade volume and the main political steps between China and the EU\textsuperscript{116}

(\textit{Unit: USD billions})

<table>
<thead>
<tr>
<th>Year</th>
<th>Total trade</th>
<th>Main political steps</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>2.399</td>
<td>The establishment of diplomatic relationship</td>
</tr>
<tr>
<td>1976</td>
<td>2.511</td>
<td>-------------------</td>
</tr>
<tr>
<td>1977</td>
<td>2.148</td>
<td>Agreement on trade and the creation of an EC-China Joint Committee</td>
</tr>
<tr>
<td>1978</td>
<td>3.284</td>
<td>Roy Jenkins, the president of the European Commission, visit China; the first EC-China Joint Committee meets in Beijing</td>
</tr>
<tr>
<td>1979</td>
<td>5.064</td>
<td>--------------</td>
</tr>
<tr>
<td>1980</td>
<td>4.971</td>
<td>----------------</td>
</tr>
<tr>
<td>1981</td>
<td>5.255</td>
<td>----------------</td>
</tr>
<tr>
<td>1982</td>
<td>4.620</td>
<td>----------------</td>
</tr>
<tr>
<td>1983</td>
<td>5.695</td>
<td>Initiating the first EC-China scientific co-operation programme</td>
</tr>
<tr>
<td>1984</td>
<td>5.882</td>
<td>First ministerial consultations take place between China and EC in framework of political co-operation. First EC development-aid package for China</td>
</tr>
<tr>
<td>1985</td>
<td>8.361</td>
<td>Agreement on Trade and Economic Cooperation between the European Economic Community and China; Jaques Delors, president of the European Commission, visits China.</td>
</tr>
<tr>
<td>1986</td>
<td>11.651</td>
<td>----------------</td>
</tr>
<tr>
<td>1987</td>
<td>11.15</td>
<td>----------------</td>
</tr>
<tr>
<td>1988</td>
<td>12.871</td>
<td>The EC delegation opens in Beijing</td>
</tr>
<tr>
<td>1989</td>
<td>23.510</td>
<td>China-EU relations are frozen because of the Tiananmen Square events in June 1989. The EU imposes a number of sanctions.</td>
</tr>
<tr>
<td>1990</td>
<td>22.160</td>
<td>Resume EC-China bilateral relations</td>
</tr>
<tr>
<td>1991</td>
<td>11.61</td>
<td>1991</td>
</tr>
<tr>
<td>1992</td>
<td>17.414</td>
<td>1992</td>
</tr>
<tr>
<td>1993</td>
<td>26.05</td>
<td>For the first time, the EU Commission provides aid to the UN Worlds Food Programme’s project in China.</td>
</tr>
<tr>
<td>1994</td>
<td>31.519</td>
<td>New bilateral political dialogue opens.</td>
</tr>
<tr>
<td>1996</td>
<td>39.698</td>
<td>The first ASEM is held in Bangkok.</td>
</tr>
<tr>
<td>1999</td>
<td>55.676</td>
<td>1999</td>
</tr>
<tr>
<td>2000</td>
<td>69.038</td>
<td>2000</td>
</tr>
<tr>
<td>2001</td>
<td>76.627</td>
<td>2001</td>
</tr>
<tr>
<td>2002</td>
<td>86.755</td>
<td>The issue of EU’s country strategy paper 2002-2006</td>
</tr>
<tr>
<td>2003</td>
<td>125.217</td>
<td>The European Commission publishes ‘A maturing partnership: shared interest and challenges in EU-China relations</td>
</tr>
</tbody>
</table>

\textsuperscript{116} The data for column two are from table 3 and the data for column three are edited from Appendix 1.
CHAPTER 5: THE PROSPECT ANALYSIS

From above discussions, it is clear that the key factors shaping China-EU trade relations are (i) the two sides’ official policy and the context of international relations (political factor) and (ii) the economic development of both sides (economic factors). According to these two indicators, there are four possibilities of the development tendency of China-EU trade relations (see graph.3).

Graph 3: Development trend model

Model ①: Implies that both politic and economic environments are in favor of China-EU trade relations. The development trend of China-EU trade relations will increase.

Model ②: Indicates that economic environment is proportional to the development of China-EU trade relations, but the political environment is not. The development trend of China-EU trade relations is unsure.

Model ③: Symbolizes that both political and economic conditions are unfavorable to China-EU trade relations. The development trend of China-EU trade relations will decrease.

Model ④: Signifies that economic factors worsen bilateral trade relations, but the political environment is favorable to bilateral trade relations. The development trend of China-EU trade relations is unsure.
It is more likely that China-EU trade relations will continue to grow, as Model ① suggests, at least in the near future. The forecast is based on the previous chapter’s research and the deduction of the future economic and political context embedding China-EU trade:

(i) A foundation to promote the healthy development of China-EU trade has been established. As has been known to all, the bilateral relations have experienced ups and downs since the establishment of diplomatic relations in 1975, but the bilateral trade has expanded rapidly and has grown steadily since the 1990s. The foundation to promote bilateral trade is based on the two sides’ common interest, both politically and economically. According to the statistical data (see table 3), the size and growth of bilateral trade volume indicates a strong foundation for China-EU trade relations.

(ii) Favorable political environment. Since the end of the Cold War in the early 1990s, the EU has seen the chance to realize its dream of a wider Europe. The EU on the one hand speeds up the process of integrating economics and politics; while on the other hand it is seeking economic, political and perhaps even military independence. Current US-EU relations are facing a challenge after the collapse of the Soviet Union. During the period of the cold war, the EU needed the US’s military protection as a deterrent to the former Soviet Union. Now the situation has changed with the collapse of the former Soviet the alliance with the US is unnecessary. It seems the EU is no longer content with taking orders from the US. The establishment of the EU can be seen as the expression of the European’s will to shake off long-term control by the US. The diplomatic strategy of the EU’s foreign policy is to lasso new strategic partners, to strengthen its presence in the world affairs, and to counterbalance the US. Belgian Foreign Minister Louis Michel said “the balance of world geopolitics has to be improved because the US is only ‘one leg of the geopolitical table’, and the EU will aim to stabilize this ‘geopolitical table’ through stimulating closer relations
between the EU and China”. On this point, the contemporary changes between EU-US relations and EU-China relations suit the neo-realist view on international relations (balance of power). The ‘stability’ of the Cold war has confirmed Waltz’s claim that a bipolar world is much more stable than a multi one, and that “in international politics, overwhelming power repels and leads others to try to balance against it”. The political closeness between China and EU is in line with this argument of neo-realism. In 1995, the EU set out its long-term policies towards China in its policy document. In 1998, the European Commission adopted another policy document ‘Building a Comprehensive Partnership with China’ and in the same year the annual China-EU summit meeting mechanism was launched, which provided the leaders on sides a chance to exchange views and cooperate closer. China’s status has been continually upgraded in EU’s diplomatic strategy from the ‘long-term cooperation relationship’ in 1995 to the ‘comprehensive partnership’ in 1998 to ‘strategic partnership of cooperation’ in 2001 and to ‘a maturing partnership’ in 2003. In October 2003, the Chinese government issued China’s EU policy paper, which “outlines the areas and plans of cooperation and measures in the next five years so as to enhance China-EU all-round cooperation and promote a long-term and stable development of China-EU relations”. The policy paper issued by China and the EU in 2003 indicates an understanding of the development of bilateral relations and builds up a favorable framework for developing China-EU trade relations in the next five years as well.

The issue of human rights has been a major theme of China-EU trade relations since the Tiananmen Square event in 1989 showing that the issue of human rights has a directly influence on bilateral trade. Generally speaking, the bilateral total trade volume will decrease when the issue of human right rises and vice versa. With further economic reform and liberalization, the degree of freedom and living conditions has

118 Amitav Acharya, “International Relations Theory and Cross-Strait Relations”.
been increasing rapidly. The Chinese authorities have recognized the importance of the rule of law in the process of China’s modernization and the country’s further integration into the international economy. The provisions relevant to the area of economic and social rights were added to the constitution in 1999.\textsuperscript{120} China’s WTO accession will further promote its human rights situation. In addition, the EU-China dialogue mechanism on human rights has been set up. It functions as a lubricant to smooth the divergence on this issue if there is any. According to neo-liberals the rules and institutions are good, because they can help states cooperate. On this point, I agree with neo-liberalist. I believe that the EU-China dialogue mechanism on human rights constitutes a platform to engage China on sensitive issues, and provides a channel for the EU and China to exchange their opinions, and create harmony among the two sides, and therefore promoting China-EU trade relations. It is reasonable to believe that the issue of human rights will not be an obstacle on the EU-China trade relations in the next coming years.

(iii)\textbf{Favorable economic environment}. Bilateral economic strength and their highly complementary economic structure is the prime mover for promoting China-EU trade relations.

\textbf{The EU’s economy}. The export growth rate of China towards the EU has been decreasing in recent years due to weak economic growth in the EU, which has led to the market shrinking. Therefore, the prospects for Chinese export depends on the future economic performance of the EU. According to the European Commission’s prediction, after a few years’ of economic sluggishness, the recovery is expected to pick up in 2004 and 2005 with accommodative macroeconomic policy conditions, continued disinflation, supportive financial conditions, progress in structural reforms and a reduction in geopolitical uncertainty.\textsuperscript{121} The EU Commission issued economic forecasts for the EU for 2003-05(see table 7).

\textsuperscript{120} The EU’s relations with China. http://europa.eu.int/comm/external_relations/china/intro/summit4.htm
Table 7: EU’s economic forecasts (2003-05)

<table>
<thead>
<tr>
<th>Year</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP Growth EU-15</td>
<td>3.6</td>
<td>1.7</td>
<td>1.1</td>
<td>0.8</td>
<td>2.0</td>
<td>2.4</td>
</tr>
</tbody>
</table>


The economic picture in the EU has started improving, with great optimism about future prospects. This is now feeding through to an improvement in the business climate and in purchasing power. Growing consumer confidence will also boost the European economy. The economy is gradually gaining momentum that should allow growth not only in 2004 but also in 2005. GDP is going to rise from 0.8% in 2003 to 2% in 2004 and 2.4% in 2005. 123 The key to the upturn is the improvement in the services sector and the manufacturing sector driven by a recovery in domestic and foreign demand. This is, in turn, expected to bring an acceleration of capital formation.

China’s economy is foreseen to resume robust growth by about 7% annually throughout the whole forecast period. 124 The outbreak of SARS and the ongoing bird flu have not affected the enthusiasm of the Chinese market. In fact, the confidence in China has increased because of the Chinese government’s quick response to deal with these issues in an open manner. China’s GDP growth, after 9.1% in 2003, is forecast a 7% growth for the Chinese economy in 2004. (See table 8).

Table 8: China’s economic forecasts (2004-2013)

<table>
<thead>
<tr>
<th>Year</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009-2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP Growth</td>
<td>7.5</td>
<td>7.3</td>
<td>7.2</td>
<td>7.3</td>
<td>7.4</td>
<td>7.2</td>
</tr>
</tbody>
</table>

Sources adapted from: Asian Development Bank (2002). 125

122 Ibid.
123 Ibid.
125 Ibid.
The optimistic estimate is based on some of the positive factors and trends that supported high growth in the past twenty years and are likely to still exist and continue to support economic growth. The positive factors, for example, are:\textsuperscript{126}:

- **High saving and investment rates.**
- **Abundant and low cost labor.**
- **Improvement of human resources.** Significant resources are devoted to education and human resources development.
- **Increasing export competitiveness.**
- **Robust domestic demand.** The huge population in China consists of the large consumer market. Economic growth has improved the purchasing power of Chinese citizens. It is forecasted that in 2005 the number of middle-income consumers will substantially increase, which is likely to boost the need for retail goods. Further, China’s goal of modernizing its infrastructure and upgrading its industries is estimated to create considerable demand for goods and services.
- **Strong demand for foreign goods and services.** Chinese officials reckon that the needs for foreign goods and services will be $1,500 billion from 1999-2005.
- **The inflow of FDI.** China will continue be an attractive market for the foreign investors because of its energetic market and accommodative macroeconomic policy.
- **The current generation of leaders: experienced; better educated; many have provincial experience**
- **Policy continuity expected**

In addition, the Chinese government in its 10\textsuperscript{th} five-year plan has set up a growth rate target that China’s GDP will grow by 7\% annually from 2001 to 2005. The GDP is expected to reach 12,500 billion yuan by 2005 while total foreign trade volume is projected to stand at $680 billion and FDI reaching $40 billion annually.\textsuperscript{127} The statistics from Chinese customs show that the growth rate is around 8\% for the period of 2000-\textsuperscript{126} \textit{Ibid.}  
\textsuperscript{127} People’s Daily (2001). China to continue pursuing active fiscal policy: Finance minister.  
2003. It has exceeded the prediction. The results for previous and the listed arguments indicate that the economic growth in China is likely to continue in the near future.

**Global economy.** The ongoing global economic recovery will create a good international environment for the EU and China’s economic growth. The European Commission predicts that the future of the world economy looks promising. World GDP growth is expected to pick up to 4.1% in 2004 and 2005 from 3.3% in 2003. (See table 9)

<table>
<thead>
<tr>
<th>Year</th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>3.8</td>
<td>0.3</td>
<td>2.5</td>
<td>2.8</td>
<td>3.8</td>
<td>3.3</td>
</tr>
<tr>
<td>Asia</td>
<td>5.9</td>
<td>4.1</td>
<td>4.7</td>
<td>5.5</td>
<td>5.6</td>
<td>5.6</td>
</tr>
<tr>
<td>Latin America</td>
<td>4.5</td>
<td>0.4</td>
<td>0.3</td>
<td>2.0</td>
<td>3.4</td>
<td>4.4</td>
</tr>
<tr>
<td>Africa</td>
<td>4.0</td>
<td>1.3</td>
<td>1.1</td>
<td>3.1</td>
<td>4.2</td>
<td>4.5</td>
</tr>
<tr>
<td>World</td>
<td>4.7</td>
<td>2.3</td>
<td>2.8</td>
<td>3.3</td>
<td>4.1</td>
<td>4.1</td>
</tr>
</tbody>
</table>

Looking ahead to 2004, the world growth is being driven by stronger the US growth, the continuous growth in Asia, and by the rebound of Latin America and Africa’s economy.

As is usually the case, much of the attention has focused on developments in the US, which has been viewed as the engine of the world economy. The data in 2002 shows a significant decline in the pace of growth, and we can see from table 9 that the GDP growth slowed quite remarkably at that time. This situation has been changed since 2002 and the growth rate remained in 2003. The momentum for growth, which is the stronger consumer spending boosted by the tax cuts, and the better performance of the manufacturing, is likely to be sustained. The European Commission offered a bullish outlook for the US economy. It estimates that the US’s economy would grow 3.8 percent this year and 3.3 percent in 2005. The Asian region also deserves some discussion here because of its outstand economic performance in recent decades and its growth impact on the global economy. Asia will continue to have the fastest growth rate, with an average 5.6 percent growth rate in 2004 and 2005 (See table 9). There are some country-specific

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factors contributing to Asian growth. In particular, the Japanese economy has been strengthened in 2003 driven by the rapid rise in import demand from a booming China and the upturn of business investment. China’s economy will grow around 7 percent this year. And Korea will achieve 5.2 percent growth due to the return of robust exports and recovering consumption. ‘Korea’s exports were projected to grow by 11.6 percent to reach $216 billion and imports to increase by 12.8 percent to $200 billion.’

Turning to another important region of the world economy, Latin America. It is predicted, led by a healthy Mexican economy, the region’s economy will have promising growth, which is expected to expand 3.4 percent in 2004 and 4.4 percent in 2005 (table 9). The last region I will talk about is Africa. The performance of Africa has been stronger. The European Commission forecasts a pick-up in growth in Africa to around 4.2 percent in this year and 4.5 percent in 2005.

In summary, China and the EU have wide-ranging interests in safeguarding world peace and stability and promoting common economic development. The recent economic data and the promising outlook entitles us to be confident about the future development of China-EU trade relations. This deduction is in line with the assumptions of neo-realism and neo-liberalism. Politically, the understanding of the balance of power leads both China and the EU to strengthen the tie between them. They have regarded China-EU ties as a means to fulfill their goal of establishing a ‘multipolar world’. It means that the US is not the dominant leader of global order. In the policy papers the EU indicates China’s status as its mature partner. Meanwhile, China in its first diplomatic paper pointed out that China-EU relation is a full strategic partnership in areas including trade, culture, technology and defense. These policy papers will be the guiding rule for the next few years. Economically, China and the EU are moving closer and closer. China, as the biggest developing country in the world, has rich human resources and a big market while the EU has the largest number of developed countries with abundant capital and advanced technology. Christopher Doucerain, member of the EU delegation of European Commission in China, outlined the next phase of cooperation, such as expanding bilateral

129 Korean economy forecast to grow 5.2%-5.8% next year.
http://koreaemb.org/archive/2003/12_1/econ/econ0.asp
trade and increasing investment, between the EU and China. The two sides enjoy a high degree of compatibility in economic, trade and technological fields. A China-EU trade relationship is a ‘win-win approach’. Ian Kay, the executive genera manager of the EU Chamber of Commerce in China, said that EU-China trade will continue to prosper and the EU is likely to become China’s largest trading partner in the near future. Bilateral commerce is expected to hit US$150 billion in 2005 and US $300 billion by 2010. Broadly speaking, although there are some issues hindering China-EU trade relations as discussed in chapter 4 (For example, the controversial dispute over the practice of anti-dumping between China-EU trades. The use of anti-dumping policy is to combat unfair competition and to protect domestic industry. This policy can easily be used as a protectionists’ instrument against free trade if it is not used properly, which jeopardize bilateral trade relations according to neo-liberalism). However, the development trend of China-EU trade is positive. In a word, the strong economic performance in the past and the promising forecast in the near future lays a solid foundation for continued high growth in bilateral trade.

\[\text{\footnotesize References:}\]

132 Ibid.
CHAPTER 6: CONCLUSIONS

This paper has focused on China-EU trade relations since 1975, with the objectives of (i) understanding and identifying the main factors determining or influencing the direction and scope of the relationship between the two countries within a broad theoretical framework and large social context and (ii) exploring the future development tendency. The analysis is based on the assumption of two international theories neo-realism and neo-liberalism.

In the neo-realist perspective, both sides take the US into account. For the EU, since the end of Cold War, it’s main concern has been (i) how to shake off the control of the US in political and economic affairs, (ii) how to become more of an independent actor, (iii) how to build a larger Europe and strength its voice in international society. As to China, it has consistently attempted to diversify its imports sources and exports market from over-depending on the US, which leads the US to easily exert political and economical restrictions. The EU becomes inevitably an important alternative for China. With these in mind, understanding of the balance of power brings the EU and China together. The closer political relations create a better economic and trade environment. Vice versa, the closer economic and trade relations contribute to tighter political relations. As to neo-liberalist perspective, trade relations are determined by the relative economic performance of both sides, by the degree of complementarity and by the mutual benefits.

Under the guidance of neo-realism and neo-liberalism framework, the paper has examined the significant developments with a particular emphasis on economic development in Asia, in China and in the EU. The development of China-EU trade relations has been analyzed closely as well. A number of conclusions can be drawn from research.

First, China-EU trade has developed very rapidly. The relations between them are good. They are each other’s third largest trading partners.
Secondly, the momentum for the development of China-EU trade relations is rooted in their common interests in both political and economic fields. Politically, China and the EU share same vision of the world order. Both of them advocate the multi-polarization of the world. Closer China-EU trade relations can offer a ground for further cooperation on international and regional security issues of mutual concern, including combating terrorism, nonproliferation. In the perspective of economy, China and the EU are strongly complimentary to each other. China-EU trade results in a ‘win-win situation’ beneficial to both sides.

Thirdly, the prospect of China-EU trade relations is promising. It is because (i) a foundation to promote the healthy development of China-EU trade has been established (for example, a set of legal framework provides both sides with the legal basis for their economic relations); and because (ii) the prediction of future political and economic environment is favorable of the development of China-EU trade relations.

It seems that trade and economic cooperation between the EU and China are better than ever. Both China and the EU define their relationship as a strategic one. The EU at the sixth EU-China summit expressed a desire to become China’s largest trading partner in the near future. All factors show optimistically that China-EU trade will continue to prosper. While China-EU trade relationship is not without friction, some potential dangerous factors may shadow the future development of China-EU trade relations and cannot be overlooked. One potential danger signal is the Taiwan issue.

The Taiwan issue has been a sensitive question in China-EU trade relations. The Taiwan issue could trigger a tense relationship between the EU and China if it is not handled properly. In 1981, for example, the Dutch RSV shipyard sold two diesel-powered submarines to Taiwan leading to a diplomatic debacle between Netherlands and China.\textsuperscript{133} It is seen by China as support of Taiwan building military power to confront China. Diplomatic relations were restored in 1984 when the Dutch Government stated that it

\textsuperscript{133} EU-Taiwan relations. http://www.ea.sinica.edu.tw/lib/abstract/30-1-3.pdf
would stop any further arms trade with Taiwan. In the early 1990s, despite pressure form Beijing, the French Government sold 16 LaFayette Frigates to Taiwanese Navy, in 1992 sold 60 Mirage fighter planes to Taiwan and in 1994 sold military hardware to Taiwan.\textsuperscript{134} In response, China closed the French consulate in Guangzhou and forbade French companies from bidding to build the city’s new subway system.\textsuperscript{135} The continued sale of arms to Taiwan from European countries harms China-EU relations and endangers China-EU trade relations as well. Moreover, the European Parliament has been an important supporter of Taiwan for joining the UN and international community. Due to the statehood of Taiwan it has not been accepted into the UN. In 2002 the European Parliament passed ‘Europe-Asia Partnership’ and within the European Parliament states:\textsuperscript{136}

``Express its concern at the arms build-up between China and Taiwan; urges both sides to de-escalate the arms build-up, and in particular for China to withdraw missiles in the coastal provinces across the Taiwan Strait...`'

It is the first time that the EU interfered into China-Taiwan issues. It has attached a very sensitive issue. One of the main principles of Chinese diplomatic policy is ‘one-China principle’. Therefore, there is no room for China to make any diplomatic compromise or concession regarding to the question of Taiwan. Any improper moves towards Taiwan by the European Parliament certainly will lead to discord in China-EU trade relations.

Another potential danger signal is the number of outstanding trade disputes between the two sides. There are numerous trade disputes, such as anti-dumping policy, tariffs and quotas, between China and the EU over textiles, TVs and agricultural products. These issues are sparking threats of retaliation that may slow and hurt trade relations. China has had a long-standing ban on importing the EU’s agricultural products. There are also textiles products and electronic products such as color-TVs that the EU wants to limit imports from China by accusing China of ‘dumping’ its products at below-market prices.

\textsuperscript{134} Ibid.
\textsuperscript{135} Ibid.
in the EU. The EU is facing increasing protectionist pressures, which trigger trade wars. These trade disputes have the potential to cause massive disruption to trade relations.

In order to further China-EU trade relation, I put forward three suggestions:

- Maintain the existing high-level of exchanges such as the annual EU-China summit. The existing mechanism is good for enhancing understanding of the leaders of the two sides through dialogue. But the dialogue needs to be more results-oriented.

- Set up a warning mechanism to prevent trade disputes escalating and provide a method for establishing negotiations. China’s accession into the WTO makes solving China-EU trade disputes under the WTO framework possible. Going to WTO dispute settlement proceedings is the final stage if both sides cannot manage to solve a particular dispute. The role of the warning mechanism is to prevent trade disputes from going too far and to leave a leeway for negotiation.

- Prevent the politicizing of trade relations. For example, do not connect human right issue with trade relations. Unrelated issues should be addressed separately.
Appendix 1: Chronology of China-EU relations

1975  The establishment of diplomatic relationship
1978  Agreement on trade and the creation of an EC-China Joint Committee
1979  Roy Jenkins, the president of the European Commission, visit China; the first EC-China Joint Committee meets in Beijing.
1983  Initiating the first EC-China scientific co-operation program.
1984  First ministerial consultations take place between China and EC in framework of political co-operation. First EC development-aid package for China.
1985  Agreement on Trade and Economic Cooperation between the European Economic Community and China; Jaques Delors, president of the European Commission, visits China.
1988  The EC delegation opens in Beijing.
1989-1991  China-EU relations are frozen because of the Tiananmen Square events in June 1989. The EU imposes a number of sanctions.
1992  Resume EC-China bilateral relations
1993  For the first time, the EU Commission provides aid to the UN Worlds Food Program’s project in China.
1994  New bilateral politcal dialogue opens.
1996  The first ASEM is hold in Bangkok.
1997  Resumption of dialogue EU-China on human rights, interrupted in spring
1996  French President Chirac visits China.
2002  The issue of EU’s country strategy paper 2002-2006

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The European Commission publishes ‘A maturing partnership: shared interest and challenges in EU-China relations; China issues its first diplomatic paper ‘China’s EU Policy Paper’
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