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LIGHTS - Geopolitics

The Future of the US-China-Europe relation

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Abstract

This work seeks to propose scenarios, based on an in-depth analysis of the literature, on the future relations between the United States of America, China and Europe from a primarily economic but also geopolitical perspective. In both the academic and policy realms, the question of what the future holds for economic relations between the United States of America, China, and Europe is one that is regularly discussed. The research done on this subject focuses on a variety of different variables that are projected to alter the ties between these three main economic powers. These drivers include economic growth, technological advancements, geopolitical conflicts, and shifting power patterns.

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The future of the US-China-Europe relation Introduction

This article addresses two primary inquiries: (i) the historical interactions among the United States of America, China, and Europe, three major economic powers, and (ii) the potential shifts in their connections, impacting the international landscape across various dimensions, including cultural and political disparities. Recognizing that economic factors alone cannot fully explain the complex phenomena driving national actions, the research delves into diverse aspects to unveil the nature of current relations and potential future trajectories. These encompass economic interdependence, the ascent of the Chinese economy, geopolitical tensions, and concerns regarding environmental sustainability. Understanding the present and forecasting the future requires a thorough examination of historical developments. Therefore the paper scrutinizes the evolution of these interactions since the second half of the 20th century and their implications for shaping the emerging global order. Presently, the relationship is characterized by both cooperative efforts and significant tensions, particularly evident in the dynamic between the US and China, which, according to the Second Cold War theory, are poised to lead two distinct civilizations. Moreover, the article offers policy recommendations aimed at informing future regulatory frameworks and long-term political strategies crucial for shaping the global equilibrium in the coming decades.

The relationship dynamics among the United States, China, and Europe are pivotal, given the constant flux in the balance of power. A comprehensive understanding of this interplay necessitates an extensive literature review drawing from diverse sources. Methodologically, this paper relies on data sourced from various global institutions, including the World Bank, with a focus on indicators such as growth rates, trade volumes, and other key variables. Numerous scholarly articles contribute to this discourse; notable examples include Andràs Inotai (2013) who elucidates the evolving dynamics of the European-Chinese relationship over recent decades. Additionally, the OECD's publication "China's Belt and Road Initiative in the Global Trade, Investment, and Finance Landscape" is instrumental in comprehending China's BRI initiative and its implications for international trade relations. Furthermore, Susanne Dröge (2021) offers nuanced insights into the complexities arising from differences in climate policies between China and Europe, necessitating enhanced cooperation to establish mutually accepted standards.

Economic Interdependence

Trade relations

In 1990, China, the US, and Europe collectively contributed to 57% of global GDP. By 2018, this proportion remained largely unchanged at 58%. However, China's share surged from a mere 1.6% to a significant 16%, providing Beijing with ample resources to narrow the gap with more advanced economies in crucial sectors like artificial intelligence, military capabilities, and energy. This transformation has conferred upon the Chinese government a substantial and decisive influence within the international arena. Notably, the volume of exports and imports between these three regions is paramount. According to the World Bank, they collectively represent approximately 33% of global exports and 40% of global imports. Over the past three decades, the Chinese economy has experienced substantial growth, with its share of global exports rising from 11% to 14%, and imports climbing from 7% to 10%. Additionally, direct trade relations between these economic powerhouses are robust. Historically, around 30% of China's trade has been with the EU and the US individually. Moreover, China's trade with the EU accounts for 30% of the latter's total trade volume, while transactions with both the EU and China combined represent up to 35% of total US trade. This article mostly focuses on the relationship between Western countries and China i.e the EU and China as well as the US and China but not the EU and the US.

Europe and China

Andràs Inotai (2013) provides a detailed depiction of how economic ties have grown over the years with China being the EU's second biggest partner. Inotai draws attention to an additional essential fact. To date, the features of the commercial ties between the EU and China reflect those of ties between highly industrialized nations. This is in stark contrast to the reputation of the Chinese economy only being able to compete minimally and only for cheap products. When the structure of trade is broken down, it emerges that almost two thirds of European exports to China consist of high-tech items such as machinery and automated equipment.

The USA and China

According to the BBC, the value of goods imported into the US from China is close to $536.8 bn while exports to China are $153.8bn and it appears that these values are on the rise. According to Xavier Jaravel and Erick Sager (2019) the benefits from the exchange of goods and services have been so significant that it has contributed to an increase of the average American family's annual purchasing power by about $1,500 in the early 2000s. Moreover, exports are found to have a direct impact on the US socio-economic condition as shown by the US-China Business Council (2017), according to which exports financially support around 2 million jobs. The American economist Arthur Laffer states that "Without China there is no Wal-Mart and without Wal-Mart there is no middle-class and lower-class prosperity in the United States". According to David Autor, David Dorn and Gordon Hanson, the "China Shock" (sum of costs incurred by the US economy as a result of increased Chinese imports) was the most significant compared to other trading partners. This happened for three main reasons. First, the fast pace at which trade increased, second, the enormous size of the Chinese labour force and its low cost and finally, the number of sectors that faced a major disruption. Moreover, the rise of Chinese know-how in technology is a major concern for the government in Washington, as Chinese companies are often accused of exploiting their relations with the US to steal the most advanced American technologies to achieve opportunistic goals. The future of the economic interdependence between the two countries is extremely controversial and difficult to predict. The forces driving China and the US are both similar and conflicting, creating strong political issues that are at the centre of international debate.

The rise of the Chinese economy

Economic reforms

The Chinese economic revolution was triggered by two main reforms: the agricultural laws and the establishment of the Special Economic Zones (SEZs). The agricultural laws (1978) broke down the socialist principle whereby farmers couldn't produce more than strictly necessary, boosting Chinese agricultural production and output which according to Lin and Justin Yifu (1992) increased by 48.21% in 9 years. In the early 1980s, SEZs were introduced. For the first time Beijing allowed strategic regions to establish restricted zones where the laws of free market and capitalism were in force. By doing so, China attracted foreign investment in the country and guaranteed important fiscal advantages. According to Douglas Zhihua Zheng (2012), SEZs generated direct and indirect benefits for the

Chinese economy. The direct benefits were a strong increase in government revenues, employment rates and exports, while the indirect benefits consisted in a general growth of Chinese industrial know-how, technology transfer and greater diversification of exported products and services. According to the World Bank, SEZs have contributed to an increase of 22% of China's GDP, 45% of total national foreign direct investment, and 60% of exports.

The Belt and Road Initiative

Currently, the largest project set up by China to increase its economic weight is the Belt and Road Initiative (BRI). The programme consists of the largest infrastructure plan of modern era, involving approximately 150 countries and aiming to connect China with the rest of the world to foster its trade partnerships. The desire to build infrastructure was prompted by the Asian Development Bank's estimate that Asia's current inadequate infrastructure costs an estimated $900bn annually. Moreover, the BRI could give the Chinese a chance to escape the so-called middle-income trap. The latter is a phenomenon theorised by economists Indermit Gill and Homi Kharas (2007), according to which emerging countries gradually lose competitive advantage by remaining stuck at an average GDP per capita estimated to be between $4,000 and $20,000. The related report published by the OECD (2018) states that the BRI will greatly expand the basin of consumers which Chinese companies can service. Considering China's total exports in 2000, only 19% were accounted for by BRI member countries, whereas today this figure has already reached 34% and according to OECD data it will continue to grow proportionally as connectivity increases. A further factor that can catalyse future trading is the creation of trading blocs. The latter could allow China to increase trade volumes with other large blocs such as the EU and NAFTA.

It is often debated whether the existence of a trade bloc produces extra-bloc benefits.. The outcomes of OECD tests are shown below.

- The regional membership is statistically significant and beneficial for the associations (ASEAN+1 and the BA) in which China participates. Therefore, it is advantageous to non-members, whether they be OECD nations or BRI participating economies.
- OECD-origin nations gain in a statistically meaningful manner, while the impact on participating economies of the BRI is unmistakably adverse.
- The link is unfavourable for SAARC-origin nations, extremely important for OECD- origin countries, and neutral in regard to the BRI. Regardless of origin, the extra-bloc benefits of NAFTA are advantageous for all nations.

Geopolitical tensions

The Second Cold War

The economic development of East Asia is one of the main factors for the increasingly marked contrasts with the Western civilisation in the last decade. Currently the growth rates of some Asian nations are reminiscent of those of Western Europe in the 19th century, and in some cases even higher. *The Clash of Civilisations* (1996), by Samuel Huntington, is a fundamental manual to grasp the path of modernisation undertaken by non-Western societies. According to the Kemalist theory, the levels of Westernisation and modernisation of a country are positively correlated. However, Huntington writes that in most cases the graph shows a bell curve, for which initially modernisation stimulates Westernisation but once a critical threshold is reached, it will begin to promote de-

Westernisation, favouring the revival of the original culture. The Chinese model confirms Huntington's theory as it appears that an exponential increase of its military and economic power (with an annual growth rate of national GDP over the last 30 years averaging 10%) has done nothing but distance China from the Western world, laying the foundations for a new form of "socialist market", characterised by aggressive economic policies. These worsened the diplomatic relations with the US and the EU, as evidenced by the tariffs imposed by the Trump administration and confirmed by President Joe Biden. Chinese power today is a dynamic force formed by the nexus of four factors: authoritarianism, consumerism, global ambitions and technology. The Chinese Communist Party has devised a strategy of great economic expansion, particularly visible in the form of recent investments in Africa, which, according to John Hopkins University, amount to $345 bn invested directly and $153 bn in loans. The funds are primarily destined for the energy, mining and transport sectors, financing a large proportion of on-site projects such as airports, highways and commercial shipping ports. However, authoritarianism could prove to be a double-edged sword for the Chinese leadership as it fosters hostility from other countries. Beijing could lose the "security umbrellas" it has benefited from in the past, with which NATO has pledged to protect its strategic assets. As an illustration, several world powers such as the US, Australia, India and Japan held joint military exercises in November 2020 to counter Chinese expansion in the Indian Ocean.

Conflicts on the global rules system

To become a full-fledged international power, China needs to grow militarily. In 2017, President Xi Jinping declared that China's armed forces will be able to compete with any other power by 2049. With a budget of $230bn (according to spokesman Wang Chao in 2023), China's investments in armaments are still significantly lower than the US ($778bn according to the Stockholm International Peace Reserve Institute) and slightly higher than EU Countries ($214bn according to the European Defence Agency). However, it must be kept in mind that Chinese military spending has grown by 76% since 2011, therefore, Xi's words are backed by critical investments that will tend to increase in the coming decades. This event alerts the West as there is a component of the Chinese leadership that is hostile to the values perpetuated in Europe and America. "Document 9", published by the Chinese Communist Party, severely criticised international organisations and harshly condemned principles such as constitutionalism, accused of being an ideological forgery. These misalignments are at the root of disagreements over the development of an international regulatory framework; without it, the ground on which international relations are built will be extremely complex and hindered.

Environmental & sustainability concerns

Climate geopolitics

Climate protection is becoming an increasingly central topic in political and economic planning. However, in the major projects aimed at boosting the Chinese economy, green standards are rarely mentioned. In contrast to the EU, whose short-term goal is to reduce emissions by 55% by 2030, the Chinese economy, following the Covid-19 pandemic, began to rely again on carbon-intensive sectors. In September 2022, the Chinese government declared that before 2030 Beijing should reach domestic emissions peak, and within 2060, the city expects to become carbon neutral. Nevertheless, international governments have raised doubts about the reliability of these targets, precisely because it is unclear how China will simultaneously stimulate its national economy and reduce its environmental impact. The People's Republic has been effective in emerging as a global economic superpower, with its share of the world income growing from 5% to over 17% in the past 50 years. However, along with this success came significant emissions which account for 28% of global volumes. This creates a fundamental problem. With China being the EU's second largest trading partner, such a revolution in the European supply chain will certainly affect the nature of the relationship between the two. Susanne Dröge (2021), makes a thorough analysis of the possible future consequences of this asymmetry and of the impacts on the international chessboard. The price of carbon, the establishment of regulations and the selection of standards (enforced domestically) will affect the trade flows between the EU and China. The bilateral relationship is getting more complicated since China and the Western nations have different perspectives on human rights and protection of intellectual property, and they are engaged in a fierce economic battle while there is a need for collaboration on climate protection.

The CBAM

The European Parliament promoted (within the Green Deal) the Carbon Border Adjustment Mechanism. The latter aims to establish a fair price on the emissions of carbon used for producing goods imported into the European Union and to foster environmentally friendly industrial production in foreign countries. The plan, which will be effective in 2026, will initially involve a few strategic sectors that contribute most significantly to air pollution and are the most easily relocated from the EU to China, such as the cement (6%) and steel (8%) industries. The performance of the CBAM reflects a declining disparity between trading partners over the medium-long term and it will be successful if it finally fades away, as trading nations emulate the EU and decrease emissions. Another benefit emphasised by Dröge is that it will increase transparency on the publication of emissions data. It is mandatory for private companies to annually provide up-to-date statistics on their activities; however there have been cases of companies trying to hide or illegally modify their data. On the other hand, the CBAM could negatively affect future relations as it could be interpreted by the Chinese authorities as a further Western attempt to sabotage exports and hinder the economic advancement of the People's Republic. The politicisation of the project could lead to diplomatic confrontation, as demonstrated by the protests already made by China (and some of its major partners such as Brazil and India) in recent international meetings.

Policy recommendations

Trade policies

The Jacques Delors Institute (2019) estimated that an EU-China trade liberalisation would increase the GDP of European nations by around 75€ bn. However, a market liberalisation with China could only be implemented in the presence of a continuous and honest dialogue between the various governments, which currently seems particularly difficult. The strong path of militarisation, increasing energy dependence on Russia, and aggressive investments in developing countries by Beijing are only making the US and EU raise their guard instead of seeking cooperation. If there is no concrete sign of improvement, this article suggests that trade policies should be implemented to mitigate economic interdependence with China in key industries.

Industrial policies

Pascal Lamy, Elvire Fabry and Nils Redeker (2022) state that 52% of the strategic military items imported by the EU come from China. Based on these figures, the Commission should issue new directives to differentiate the procurement of European nations. Further action should be taken in the industrial sector to improve its efficiency. For this to happen, action must be taken on two fronts. First, create a stronger industrial policy framework, especially in terms of governance. Secondly, we propose to build a common industrial fund, as different member countries have significant diverse economic availabilities. In this way it would be possible to finance projects which have strategic value for the Union, consequently reducing the economic gap between the various nations, which is often at the root of internal conflicts that prevent the EU from having coherent and effective policies.

Energy policies

The Intergovernmental Panel on Climate Change (the main UN body focused on climate change) published a report in 2023 reaffirming that human practices, particularly the use of fossil fuels, are the main cause of rising temperatures. UN Secretary General Guterres said that "humanity is on the brink and there is a real risk of defusing a time bomb". Faced with such a scenario, future policies will have to be written in terms of strong cooperation between countries, as there is no viable alternative. To make this happen, it will be necessary to promote global agreements (such as the Kyoto Protocol or the Paris Agreement) through which guidelines will be outlined for the future. Goals such as seeking to keep the average temperature rise at +1.5 degrees Celsius compared to the pre-industrial era will have to be signed and adhered to by all powers, including China, to avoid an environmental catastrophe. Furthermore, achieving these ambitious targets will require the introduction of new policies to encourage technological investments to speed up the decarbonisation process. In 2022, for example, the US-China Working Group met for the first time and shared possible strategies to work together on new forms of clean energy sources with substantial investments from both countries.

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