



Foreign Trade Association

FTA Position on EU – China Trade Relations

The FTA is the association for European commerce that specialises in foreign trade issues. It is committed to achieving its goal of a true free trade environment. For almost 30 years it has supported its members, consisting of national trade associations and companies from all over Europe, by providing expertise and up-to-date information and by campaigning on their behalf against protectionist measures in the European and international arena.

Introduction

In 2005, imports from China (incl. Hong Kong) accounted for more than 50% of the imports by European retail traders from countries outside the EU. 25 years ago this figure amounted to a mere 2.5 %, which means that since then, China has produced the highest and most constant growth rates of all FTA supplier countries. However, the balance of trade with China shows a deficit of €106.3Bn, which from the point of view of the national economy is not satisfactory. These figures already show that utmost importance must be attached to the relations between the EU and China.

1. The different aspects of China's growing importance for the EU

- **Growth** - China's advancement gives new impulses to the growth of the world economy and accordingly has an impact on investment activities and trade flows. Thus the expansion of world trade always results in an overall growth of the national economy, too.
- **Competition** – The increasing competition between European and Chinese enterprises forces the European economy to make structural adjustments and increase its efforts in the field of product innovation. This results in an increased competitiveness also with regard to other third countries, which again has a positive impact on the European retail trade.
- **Investments** – Owing to China's increasing economic growth, the chances to make profitable investments in China are improving. This is also to the benefit of European producing and trading companies.
- **Research and development** – The increasing competition urges European companies to drive forward research and development. This also has signalling effects on other sectors where the economy of the European Union is still fully competitive.
- **Price development** – The increasing competition and comparably low import prices have had a positive effect on the price development within the European Union. The purchasing power thus maintained will also be beneficial to the European economy.
- **Political stability** – As a rule, economic growth is also supporting the political stability of a country. This also supports such a transformation process from a centralized to a market economy, which is currently taking place in China.

In spite of these quite convincing positive effects of China's upswing for the European economy and also European trade, there are still a number of risks involved in the new relations with China, and we should be aware of them. The following aspects are of particular relevance:

- **Protectionism** – China, being the most important supplier country for textiles and clothing products, was hit especially hard by the restrictions under the Agreement on textiles and clothes. Contrary to the original scheduling, the protection against China in the clothing sector will continue until 2008. This is accompanied by the obvious trend to impose restrictions on the import of consumer goods from China.
- **Political influence** - China is increasingly becoming one of the world's economic superpowers. This will automatically result in an increase of the country's political importance, the impact of which for the time being is hard to assess.
- **Raw material and energy markets** – China's increasing demand for raw materials and energy will result in a shortage of non-renewable resources, which will lead to a rising price level on the world markets. As a consequence, in countries short of raw materials, among which are all countries of the European Union without exception, inflation will rise beyond proportion, so that the consumers' purchasing power decreases. This in particular will have a negative impact on trade.
- **Violation of intellectual property rights** – There is no other country in the whole world where intellectual property rights are violated as often as in China. This situation will result in a weakening of the competitiveness in those product segments where European entrepreneurs are still maintaining a leading position.
- **Loss of jobs** – Owing to the wage level being considerably lower in China, European producers will keep moving jobs to China. While this can save the continuity of European enterprises on the one hand, it will result in a loss of jobs and thus of purchasing power in the European Union on the other.
- **Dependence on China** – Too much of focussing on China as a supplier country will create a dependence which will have negative effects on other supplier countries and in the case of a crisis may put into danger an adequate supply of goods to the EU. In this context we would like to mention:

- Political crises, triggered off by a limitation of existing democratic basic rights
- Social crises, triggered off for example by an army of 200 million migrant workers with a monthly income of 30 to 50 Euro and by the extremely high unemployment rate among the rural population (30 per cent)
 - Epidemics like SARS
- Severe ecological problems resulting in an inability to supply the majority of the population with clean drinking water.

2. What are the most important opportunities for Europe in China's economic growth and greater weight in international trade?

2.1 China is one of the most important sourcing countries for EU retail

European commerce plays an important role in the EU economy. The commerce sector provides for 27 million jobs and generates 13% of European GDP. Already today traders have established close business relations with Chinese suppliers of consumer goods. A further strengthening of trade relations with China will support the expansion of businesses and help create new jobs. The distribution sector could contribute much more to the economic growth in Europe as it is for example in the United States.

Nonetheless, retail trade is still handicapped by numerous trade defence measures against consumer goods from China (textiles, clothing, footwear, ironing boards, bicycle seats, canned mandarins, plastic bags, furniture, etc.). As can be seen from the textiles and clothing sector (T&C) there is much more potential for international trade. A more open market in China for highly sophisticated T&C products would give many new opportunities for exports from the EU. On the other hand, there would be manifold opportunities for imports from China. However, at present certain clothing categories are subject to a quota regime until the end of 2007 and (provisional) anti-dumping duties have been imposed on footwear. Further safe-guards and anti-dumping procedures are possible and probable. These measures are not always justified and are sometimes merely intended to shelter out-dated European industries from competition and structural change.

However, increased competition would force manufacturers to innovate which would lead to growth and job creation in Europe. Artificial prevention of competition through protectionism prevents this mechanism. This can be seen in some EU member states where parts of the manufacturing industry – under the shelter of the WTO Agreement on Textiles and Clothing (ATC) – have failed to

develop and adapt to the needs of the world market. As a consequence, the companies may have to close down and leave many people without job once the protective measures stop.

2.2 The BSCI aims at improving social standards in the supply chain of European retail

In 2003, the FTA initiated the Business Social Compliance Initiative (BSCI) with the goal to improving social standards in the supply chain of European retail. Today, a prominent number of leading European retailers participate in this initiative. A joint code of conduct based on ILO (International Labour Organisation) core labour standards is part of the buying conditions. Compliance is controlled by independent auditing companies. BSCI members have already initiated several hundred audits in China. They support training and coaching measures for companies, management and workers and therewith noticeably contribute to the improvement of working conditions.

This private initiative offers the most effective tool to enforce better social standards in supplier companies in China as BSCI members not only monitor the social compliance of their suppliers but also support the improvement actively. The more European retailers get involved in EU – China trade the more they can and will contribute to the improvement of social standards in China.

2.3 China as an important exporting and investment country for EU retail

Not only is the number of “nouveau riche” Chinese consumers steadily increasing but with the improvement of the economic level of China the general buying power is increasing. This development offers promising market opportunities for European retailers, mainly for up-market products. Moreover, European retailers have developed efficient retail concepts which can also be implemented successfully in China. Already large retail companies like Carrefour, Metro and Auchan have brought their retail concepts to China and operate in the Chinese market. Also smaller retailers are looking to China as a promising market. With its growing economic potential and the ever growing buying power, in the future China will be an interesting investment country for European retailers.

3. How should the European Union respond to the challenges originating from China?

Basically the European Union should regard China’s advancement as a positive challenge and make use of the advantages of the existing potential instead of cutting off its markets and taking protective measures.

We therefore would like to make the following **recommendations**:

- **Improvement of market access** – The access of goods, services and investments to the Chinese market must be improved. This is why the EU should urge for a strict compliance with the relevant WTO rules. Apart from that, China should ensure the mutual recognition of testing results on the basis of well-established international standards, so that one-time testing of a product will be sufficient for the world market. Also on local and regional and levels the consistent application of Chinese laws must be provided for in order to prevent them from being misused as subtle instruments for the limitation of an access to the market.
- **Protection of intellectual property rights** – European companies are suffering sales losses in China, because copies of their products are being offered on the Chinese market. Moreover, both industry and trade have their images damaged due to the lower quality of the copied products. Action against product piracy must be facilitated and in any case the enforcement of claims for damages and default claims according to civil law must be ensured.
- **Liberalisation of the service sector** – The proper functioning of the service sector is of growing importance for China. However, there are still many restrictions and burdensome requirements for foreign companies. Therefore, the EU should urge China to implement its WTO commitments to open the retail sector and wholesale services. Also the functioning of other service industries like insurance, banking and telecommunication must be secured as these sectors are important for commerce and industry.
- **Raising of awareness for WTO rules** – The European Union should, as a matter of principle, raise the Chinese government's awareness for the possibility of dispute settlement on both WTO and bilateral levels. That way trade disputes could be settled without political or economic implications.

- **Support of certain branches of industry** – The endeavours of certain branches of the European consumer goods industries to drive forward innovation, restructuring and an improved market access to China must be flanked by political support. The High Level Group on Textiles and Clothing established by the European Commission is an expedient example of such political support. Among other things it has worked out concrete recommendations for structural improvements in the textiles and clothing industries as well as in the field of research and development. This is not only benefiting the textiles industry but the whole sector, including the textile trade.
- **Development of an Asia strategy** – The European Union should develop a strategic concept concerning its relations with Asian countries, covering not only China but also other Asian countries, in order to prevent too big a dependence on China as a supplier country. In doing so, the aspects of free trade should be given highest priority. As the case may be, bilateral free trade agreements could be concluded with certain Asian countries or regions.

4. Conclusions

The past has shown that protectionism is the wrong path. The EU economy must adapt to the new market conditions and transform to a more services oriented economy. Some well known EU textiles and footwear brands already today provide thousands of jobs in the EU without producing here. They have outsourced their production to China or other Asian countries but offer countless jobs in their European headquarters that focus on product development, design, logistics, administration, etc.

However, an important precondition for these huge EU manufacturers is a prominent number of sales. To achieve this, EU companies need new market opportunities in third countries. China has all the potential to fulfil this need. In order to let manufacturers benefit from their competitive advantages, their intellectual property needs to be protected.

Regarding the improvement of social standards the EU as well as the Chinese government should support and promote private sector initiatives like the BSCI.

For the sake of development and poverty reduction in China, the EU should ensure that trade barriers in the EU for China are kept to a minimum. It should help European retailers and manufacturers promote the high quality of EU goods.

In view of China's outstanding importance as an economic partner of the European Union it is necessary to attach specific importance to the relations between the EU and China. China's upswing creates numerous chances as well as risks for the European producing and trading

companies, and the EU's ability to influence these chances and risks is only limited. As far as risks are controllable, the EU should refrain from exaggerated trade defence measures against China. Such measures not only will harm European trading companies and limit competition, but will also evoke retaliatory measures by China.

In the debate on China, we urge the principle parties to refrain from panic mongering and exaggerated reactions, but to keep in mind the long term interests of the European Union and the advantages of stable bilateral economic relations on the basis of mutual benefit.

Brussels, June 2006