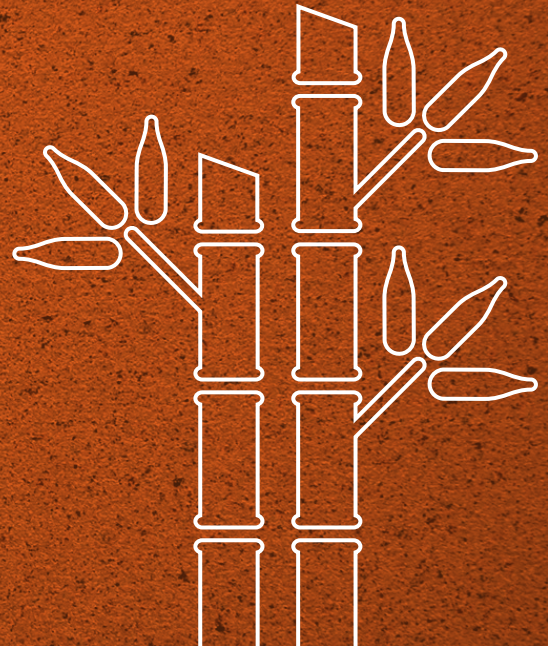


The End of Panda Politics

Bernhard Bartsch



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Somewhere in the bamboo forests of China's Sichuan Province, two pandas are being readied for their journey to Germany. The animals are to accompany Chinese President Xi Jinping when he visits Berlin next year, and will serve as goodwill ambassadors in the city's zoo. Everyone loves pandas: They are cute, vulnerable, peaceful and vegan. Policymakers in Beijing would like nothing more than for the world to feel for China at large the kind of sympathy it affords the country's national animal. "Panda diplomacy" has therefore long been a part of the country's soft-power portfolio.

Not only are the creatures themselves highly symbolic, but so are the arduous negotiations that have preceded their dispatch. Germany's first pandas were simply a state gift, given to then-Chancellor Helmut Schmidt in 1980. Their successors, however, have required many years of detailed discussion at the highest levels in order to address the many political conditions, the legal framework and the considerable sums of money involved. (This time the pandas are not a gift from China, but are being loaned to Germany as part of a specially organized bilateral research project.)

The pandas are the warm and fuzzy part of German-Chinese relations. In other areas, the contact has become less pleasant, a development that Germany's politicians and business community observe with growing unease. For many years the relationship was reciprocal: Germany's innovative power and China's modernization complemented each other perfectly. Now, however, there is a greater awareness of the economic

and political competition between the two nations—and of the conflicts that could result.

Diplomacy and well-functioning business partnerships demand that discord be avoided if at all possible—and for good reason. Yet when they are able to speak freely, Germany's managers and politicians are now asking how much longer they can count on German-Chinese relations to remain harmonious and how Germany should position itself vis-à-vis China in the future. Until now, the instruments available to serve Germany's considerable interests have been weak at best.

Special Relationship with Cracks

Germany still enjoys a special relationship with China, each country playing a key role for the other politically and economically. No other European nation has more extensive ties to China. The two countries jointly organize more than 50 programs and events for promoting dialogue, including prominent government consultations. As part of the consultations, German Chancellor Angela Merkel traveled to Beijing in June, accompanied by six cabinet members and five state secretaries. In addition, Germany is the only country with which China regularly holds cabinet meetings at the highest level of government.

Economically, the two countries are the most important trading partner each has on the other's continent. Exports to the People's Republic account for approximately 2 percent of Germany's gross domestic product. For many German corporations and mid-sized technology firms, China is a

German-Chinese Dialogue Mechanisms



List of Abbreviations

Germany:

AA – Federal Foreign Office
 BAKS – Federal Academy for Security Policy
 BGR – Federal Institute for Geosciences and Natural Resources
 BMAS – Federal Ministry of Labor and Social Affairs
 BMBF – Federal Ministry of Education and Research
 BMUB – Federal Ministry of Environment, Nature Conservation, Building and Nuclear Safety
 BMEL – Federal Ministry of Food and Agriculture
 BMFSFJ – Federal Ministry of Family Affairs, Senior Citizens, Women and Youth
 BMG – Federal Ministry of Health
 BMI – Federal Ministry of the Interior
 BMJV – Federal Ministry of Justice and Consumer Protection
 BMVg – Federal Ministry of Defense

BMVI – Federal Ministry of Transport and Digital Infrastructure
 BMWi – Federal Ministry of Economic Affairs and Energy
 BSH – Federal Maritime and Hydrographic Agency
 BfN – Federal Agency for Nature Conservation
 DAAD – German Academic Exchange Service
 GfZ – Federal Agency for Nature Conservation
 DFG – German Research Association
 DPMA – German Patent and Trade Mark Office
 PTB – National Metrology Institute of Germany
 SPD – Social Democratic Party of Germany

China:

ACYF – All-China Youth Federation
 AQSIQ – General Administration of Quality Supervision, Inspection and Quarantine



CASS – Chinese Academy of Social Sciences
CPC – Communist Party of China
CRAES – Chinese Research Academy of Environmental Sciences
CSB – Chinese Seismic Bureau
LAO – Legislative Affairs Office of the State Council, P. R. China
MEP – Ministry of Environmental Protection
MIIT – Ministry of Industry and Information Technology
MOA – Ministry of Agriculture
MOD – Ministry of National Defence
MoE – Ministry of Education
MoF – Ministry of Finance
MOFCOM – Ministry of Commerce
MoH – Ministry of Health
MoHRSS – Ministry of Human Resources and Social Security

MoHURD – Ministry of Housing and Urban-Rural Development
MoST – Ministry of Science and Technology
MoT – Ministry of Transport
MPS – Ministry of Public Security
NDRC – National Development and Reform Commission
NEA – National Energy Administration
NIM – China International Institute of Metrology
NPC – National People's Congress
NSFC – National Natural Science Foundation of China
PBOC – People's Bank of China (Zentralbank)
SAC – Standardization Administration
SIPO – State Intellectual Property Office of China
SOA – State Oceanic Administration

make-or-break market. More than 5,000 German companies are currently active in China, and more than 1,000 Chinese companies operate in Germany. For many years, Chinese have been the largest cohort of foreign students enrolled at Germany's institutions of higher education (currently some 23,000) and are thereby establishing a growing network of connections on both the personal and societal levels.

China is defending its interests with growing constancy and insistence. Beijing has a right to do exactly that, but it is forcing Berlin to reconsider its own interests and how it will pursue them.

The political, economic and social ties now are so close that it is hard to imagine a fundamental upheaval in the countries' relations because of a single conflict. Yet the more the relationship develops, the more complex it becomes. China is hardly a panda strolling peacefully across the global stage. The country is defending its interests with growing constancy and insistence. Beijing has a right to do exactly that, but it is forcing Berlin to reconsider its own interests and how it will pursue them.

Three current issues illustrate the cracks that threaten to undermine the harmony that has previously been the hallmark of German-Chinese relations.

1. Kuka

This summer the name Kuka became synonymous with the question of how welcome Chinese investment is in Germany. The robot manufacturer Kuka is considered a key player in Industry 4.0, Germany's strategic initiative to combine manufacturing and high-tech. Seeking to acquire the company, the China-based Midea Group made Kuka's shareholders an attractive offer, stoking fears that the Chinese could gain access to Germany's core know-how—and not just at Kuka, but also at firms such as Daimler and Siemens that use Kuka robots in their production lines.

The German government went to work behind the scenes to assemble a consortium of German players that could make a counteroffer and ensure Kuka remained in German hands. Rumors spread that Berlin might hinder a foreign takeover by dragging out the approval process for years. Critics accused the government—in particular Economics Minister Sigmar Gabriel—of protectionist behavior, thereby chipping away at the cornerstone of Germany's economic policy, namely support for free markets. Can Germany adhere to this principle when dealing with a major economic power that uses protectionist barriers to shield many of its own economic sectors?

Gabriel's efforts prompted considerable displeasure in Beijing and ultimately failed at home because of the disinterest exhibited by German industry and the country's shareholding laws. The steps Midea will take as majority owner remain to be seen. Yet as China aggressively expands into world markets, there will be an ongoing discussion about the difference between engaging in protectionism and ensuring business locations remain viable, a discussion that will undoubtedly feature—contentiously—in German-Chinese relations.

2. Market Economy Status

Similar concerns underlie the debate about whether China should be granted market economy status (MES), something Beijing demands the EU do by December 2016. China justifies the move based on the country's 2001 accession agreement to the World Trade Organization (WTO). If MES is awarded, it would be more difficult for European companies to defend themselves against Chinese price dumping. The decision to grant MES will be made at the EU level; Germany, however, has a strong voice in the matter.

Policymakers in both Berlin and Brussels are frustrated that their various options are unsatisfactory. On a substantive level, a broad consensus exists that China does not meet the requirements for MES. Businesses complain about conspicuous asymmetries in the competitive conditions that foreign firms face in China and that Chinese companies find in Europe—for example, in terms of rule of law, the awarding of contracts for public projects and openness toward investment.

At the same time, Germany and other EU members must concede that, from a legal perspective, China has a number of solid arguments on its side. Conversely, China's chances of winning are generally perceived as slim were it to contest its case at the WTO. If they want to avoid a trade war with China, the Europeans will, for the most part, have to accommodate China's request—and begin looking for new trade-protection mechanisms that do not violate WTO regulations.

3. South China Sea

Although China insists on adherence to international law when it comes to being granted market economy status, it is more than willing to dismiss international jurisprudence when

the issue is sovereign rights in the South China Sea. In July, the Permanent Court of Arbitration in The Hague rejected most of China's claim to territory near the Philippines and Vietnam. Although China has signed the UN Convention on the Law of the Sea, it refuses to accept the ruling. As a result, the conflict with its neighbors and with the United States, which maintains a military presence in the Pacific, threatens to escalate.

Although Germany's policymakers and business community are happy not to be directly involved in the dispute, Berlin is forced to watch from the sidelines as a conflict brews in East Asia, a conflict that has the potential to destabilize one of the globe's most important economic regions. China's outright rejection of the ruling in The Hague also demonstrates how difficult it is to include the country in international governance mechanisms—something Germany has a fundamental interest in doing.

Scenarios for China's Development

The current debate goes beyond demonstrating where the potential for tension exists in German-Chinese relations. At least as important as individual examples of discord is the general uncertainty surrounding the direction China's development will take. For a long time—too long, from today's perspective—Germany's political and business leaders acted on the assumption that the Chinese system would converge with the Western model over the medium term. The trend toward a less regulated economy, stronger rule of law, an ongoing opening to the rest of the world and, to some extent, a weakening of political control seemed irreversible. Such assumptions were what allowed Europeans to assert that China could be recognized as having a market economy within 15 years. They presumed it would happen as a matter of course.

Now, however, in the Xi era, that certainty has largely dissipated. China finds itself in a phase of structural upheaval instead. The degree to which China does or does not succeed in transforming itself will also impact its relationship with Germany.

In order to better understand long-term strategies for dealing with China, the Bertelsmann Stiftung and the Fraunhofer Institute for Systems and Innovation Research identified several scenarios of how things in China could develop through 2030.¹ From the German perspective, three scenarios are equally troubling:

- In the **Status Quo scenario**, China's political and economic system remains largely stable. Accordingly, China would continue to be a difficult but relatively reliable partner for German companies and policymakers.
- In the **Chinese Dream scenario**, China's government successfully implements its ambitious economic reforms. This would make the country more of an economic competitor

for Germany, but also a continued growth market and stable political partner.

- In the **Great Wall scenario**, several of the current problems escalate, causing China to become isolated, similar to what has happened with Vladimir Putin's Russia. German-Chinese relations would suffer, as would the German business community.

What all the scenarios have in common is that dealing with China will become more of a challenge. Another commonality, however, is that Germany can benefit from all of the potential developments if its business and political leaders respond appropriately and soon. Although it is not possible to formulate a concise strategy for dealing with China, several opportunities exist that will play a crucial role in determining how German-Chinese relations evolve.

Focus Areas for Germany's China Policy

1. International Governance

Regardless of how China develops, Germany has an interest in including the People's Republic to a greater degree in international governance mechanisms so that Beijing can take on more responsibility addressing global issues—for example, in the G20, diplomatic coalitions formed to overcome current crises or at the UN. China has publicly expressed the desire to become a leading world power, yet it remains unclear to what extent it can take on this role within existing structures or wants to make use of its own parallel institutions.

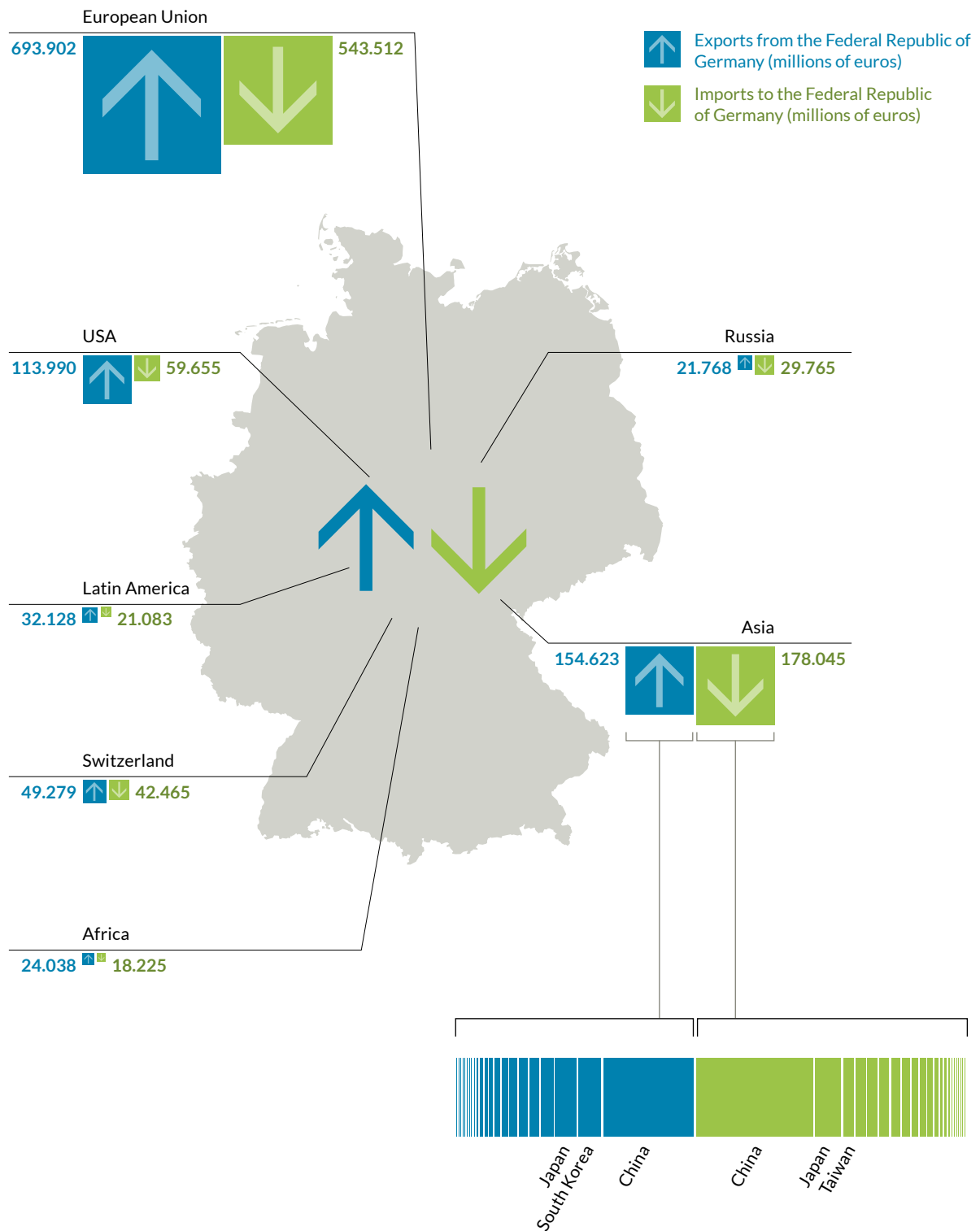
China is skeptical of existing institutions for global governance because it does not feel it is adequately represented in them. Parallel institutions such as the Asian Infrastructure Investment Bank (AIIB) or the Shanghai Cooperation Organization (SCO) diminish the influence of traditional institutions. The degree to which Germany should participate in these Chinese initiatives is, diplomatically, a sensitive topic. On the one hand, Germany has an interest in maintaining and strengthening existing mechanisms. On the other hand, it does not want to be excluded from the new organizations in the event they become generally accepted.

In the case of the AIIB, Germany decided to become a member, in part to exert influence on the bank's development. The establishment of the AIIB is, however, a good example of how China is able to play Western nations off each other, as the United States tried until the last minute to prevent the new organization from being accepted as a serious alternative to institutions such as the World Bank and the Asian Development Bank.

2. Political Alliances

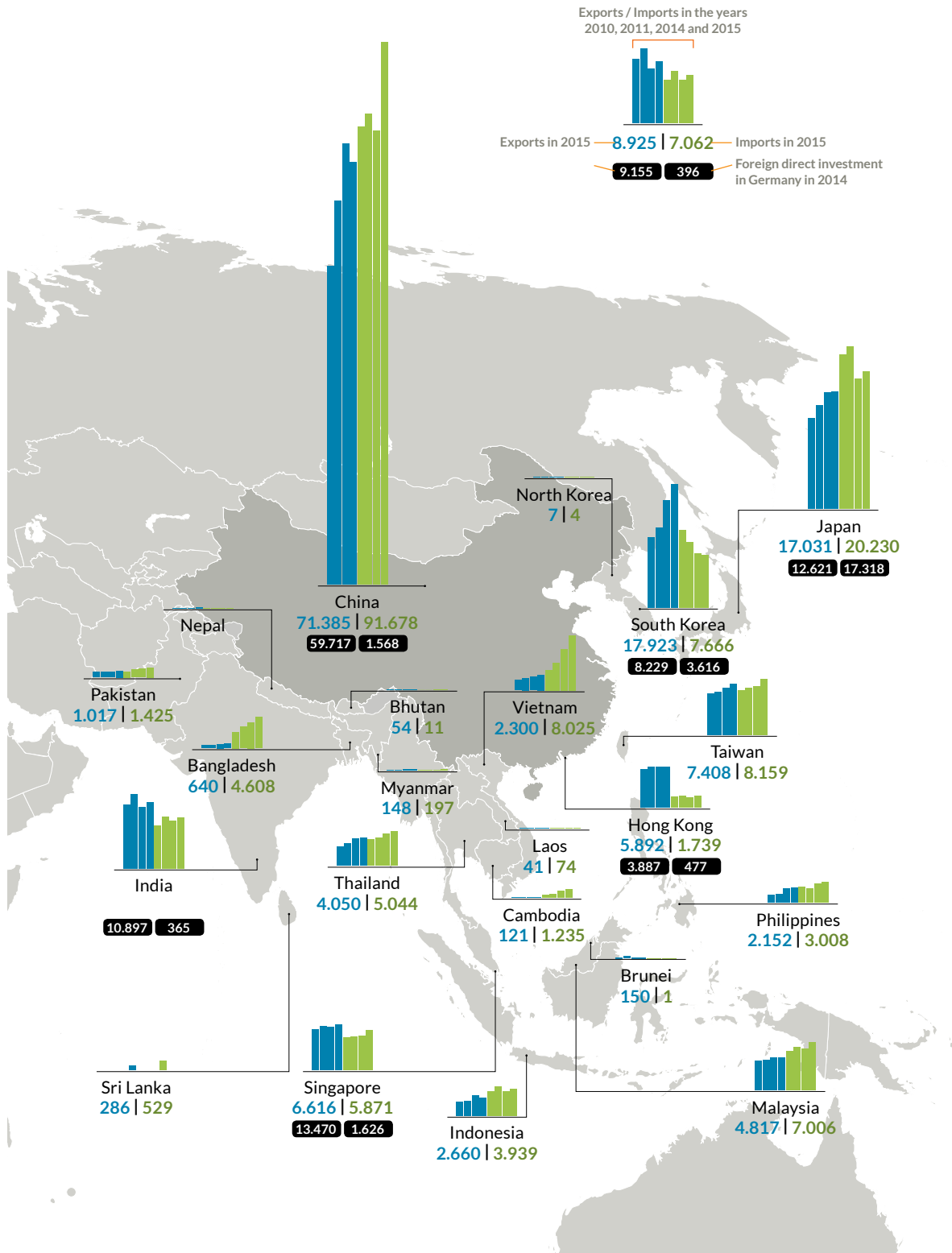
As much as Berlin has benefitted from and wants to maintain its special relationship with Beijing, it will not be able to count on receiving preferential treatment over the long term. In all of

Exports from and Imports to the Federal Republic of Germany, 2015



Source: German Federal Statistical Office (DEstatis) https://www.destatis.de/EN/FactsFigures/NationalEconomyEnvironment/ForeignTrade/TradingPartners/Tables/OrderRankGermanyTradingPartners.pdf?__blob=publicationFile

German Exports to and Imports from Asia



Source: German Federal Bank, "Bestandserhebung über Direktinvestitionen", April 2016

the scenarios examined, as a mid-sized power Germany would gain in the coming years only if Europe had a coordinated, effective foreign policy in place with regard to the People's Republic. There are many reasons why the EU's existence should be safeguarded, China's rise being one of them.

China's development is changing the international power structure. In order to be heard within it and to secure its own interests, Germany would be well advised to seek new coalitions, such as with other Asian countries. This applies both if China's global political and economic influence increases, and if China becomes involved in international confrontations. Forging new alliances is, however, not without its risks. China mistrustfully monitors where partnerships emerge around the world, especially when Beijing suspects such partnerships could offset its own increasing importance and might be designed to contain it.

3. Promoting Reform and Upholding Values

Germany has a strong interest in China's stability and having an effective government. Moreover, stability and reforms are mutually dependent: In the past, China's stability was the prerequisite for the reforms successfully implemented in many areas. In the future, it will only be possible to maintain stability if additional reforms are carried out. There is no lack in China of ambitious, intelligent goals for revitalizing the country. Yet great uncertainty exists as to whether Beijing is indeed on the right path to achieve these goals—and quickly enough to keep pace with its growing challenges.

In the past Germany has supported China's reform policies in many areas, and it should continue doing so. However, this includes recognizing that China's reformers are not only to be found among its politicians. Human rights activists and critical journalists are regularly subjected to repressive measures; openly supporting them is politically risky because China's government views this as interference in its internal affairs. Conversely, not supporting them heightens the risk of hindering reforms instead of promoting them. All of the scenarios that envision successful reform show that progress in this area is not possible without better rule of law, a system of values that espouses freedom, and a lessening of restrictions on digital media.

Maintaining a balance between pursuing interests and upholding values is one of the toughest challenges Germany's policymakers face in dealing with China. The German public expects the country's leaders to actively defend Western values such as democracy, freedom of expression and freedom of the press. China's government resists counsel offered by Western nations and sanctions countries that get too involved in its internal affairs. Defending Germany's values without endangering its business or economic interests is a balancing

act that the country's diplomats will have to maintain in all of the scenarios likely to develop in the coming years.

4. Innovation

Regardless of how China develops, the competition to remain a leading innovator will be a key factor determining Germany's future prospects. Germany's economic strength stems from the innovative power of its businesses. For the most part, Germany alone will decide if it retains this competitive edge. The competition, however, is growing. China is investing enormous sums of money to catch up with the world's innovators, especially in sectors in which Germany has traditionally excelled, such as mechanical engineering, renewable energy and hybrid vehicles.

Regardless of how China develops, the competition to remain a leading innovator will be a key factor determining Germany's future prospects

This plan has only been partially successful until now, although China has become a global leader in a number of industries including telecommunications technology and high-speed trains. In any event, the new competition is forcing German industry to develop more products faster and better in order to maintain the innovative advantage of offering goods "Made in Germany." The country's policymakers must make this possible by putting the relevant educational policy framework in place.

Should China succeed in becoming an innovation leader in the relevant industries, it would be a serious competitor for German firms and, at the same time, a business location that offers many promising opportunities. If Germany's businesses want to benefit from China's innovative power and have access to its brightest and best, they must make their Chinese employees and research centers an integral part of their global development strategies.

First movers would have a considerable advantage here. Until now, however, few German companies have been confident

to transfer their core knowledge to China. Such a step will only pay off when the People's Republic achieves a truly level playing field, one that effectively protects intellectual property rights and ensures open access to the country's markets. This development can only be expected in the scenarios that assume the greatest willingness on the part of China's leaders to introduce reforms.

5. Free Trade and Investment

As a major exporter, Germany has a core interest in promoting free trade. China will remain an important sales market for its products. How the global trade regime develops will also determine the options Germany has for further reducing trade barriers. New breakthroughs seem unlikely within the framework of the WTO. Therefore, Germany should pursue additional European free trade agreements (FTAs) in order to prevent German exporters from being disadvantaged by other bilateral or regional FTAs. One possibility is a European-Chinese FTA, in particular one that also reduces non-tariff barriers.

Chinese foreign investment is increasing and as long as the country prospers economically, this trend is likely to continue. This activity stems, on the one hand, from the desire to profitably invest foreign currency holdings, for example in real estate. On the other, it is part of a strategy to create global corporations based in China, for example through the acquisition of successful Western companies. The latter goal, in particular, is controversial.

The extent of future political and economic resistance depends largely on how China is perceived on the international stage. Germany, however, has a fundamental interest in attracting Chinese capital. It can increase its appeal by reducing bureaucracy and doing more to market itself as an advantageous location for business.

A Final Word

China and Germany are key partners for each other. Their economic, political and social ties are closer than ever before. This is a welcome development, since Germany and China need each other: as markets and fair competitors, as political allies working to address global challenges and as sources of social inspiration.

The closer connection means, however, that never before has so much been at stake. The German and Chinese economies no longer simply complement each other, but increasingly compete with one another as well. That is a natural development. Conflicting interests in the political sphere must also be expected. At the same time, both Germany and China face enormous pressure to implement reform. The stress in each of their systems is also being felt in their bilateral relations.

Germany should prepare itself for disputes with China that are more difficult than those of the past. Until now, the two countries have had little experience dealing with such situations. The challenge will be to create structures that make it possible to endure these conflicts and prevent them from spilling over into other areas. This will require Germany to become more aware of its own interests and to develop instruments capable of achieving them. That might be painful, since it could disrupt what has previously been a harmonious relationship. It will also require recognizing that Germany's options for taking action where China is concerned are often limited. After all, German-Chinese relations involve much more than just pandas frolicking in a zoo.

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ABOUT NEWPOLITIK

Newpolitik provides in-depth analysis of German foreign and domestic policy issues for policymakers beyond Berlin.

Citations

- 1 *China 2030: Szenarien und Strategien für Deutschland* (China 2030: Scenarios and Strategies for Germany). Bertelsmann Stiftung, June 2016.

Further Reading

China 2030: Szenarien und Strategien für Deutschland. Bertelsmann Stiftung, June 2016.

The Bertelsmann Stiftung has made an online tool available in conjunction with this study. It allows users to compare their own expectations of how China will develop with those of the experts: <https://china-szenarien.bertelsmann-stiftung.de>

More than a Market—How German companies are growing roots in Chinese society. Bertelsmann Stiftung, May 2016.

Jabin T. Jacob. *Wirtschaft im Abschwung? Der Blick Asiens auf China*. Bertelsmann Stiftung, April 2016.