

# CER Bulletin

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# Why the EU can be tougher on China

by Zach Meyers and Sander Tordoir

EU policy-makers have dithered over their approach to China and Taiwan. They must persuade Beijing that the economic consequences of an invasion would hurt China, but be bearable for the EU.

Relations between America and China are dire. Democrats and Republicans differ on almost everything, except that the US should impede the growth of China's military capabilities, and remove America's biggest economic dependencies on China. One flashpoint in US-China tensions is the contested status of Taiwan, which Beijing sees as a renegade province. Washington fears that Beijing may soon invade the island.

The US Inflation Reduction Act tries to remove China from strategic supply chains entirely. The EU seems to have uneasily accepted that it needs to 'de-risk' trade, by diversifying its suppliers in specific sectors. This gives the EU and US positions some superficial similarity. But it is unclear how serious different EU member-states are about de-risking or what they mean by it. German Chancellor Scholz and French President Macron both took an entourage of CEOs on their visits to China in recent months, signing new business deals. The Netherlands agreed to strengthen controls over the export of high-end chip-making equipment to China, but it did so reluctantly, only at Washington's urging. The Netherlands is now trying to present its rules as non-discriminatory so as not to anger Beijing.

Staying out of US-China disputes might seem safest for the EU. Though only a handful

of European firms have significant direct investments in China, it is the EU's third-largest export market. For example, car exports to China make up about 1 per cent of German GDP. A conflict over Taiwan would threaten European exporters: the EU would face huge pressure from the US to impose sanctions. China is also the EU's largest source of goods imports, and a conflict could result in Beijing blocking exports of critical materials used in countless European industries. The [IMF](#) estimates that if the global economy fragmented into blocs, as might occur after an invasion of Taiwan, the EU would be better off if it did not align with the US, for example by continuing to trade with China.

Such an approach – and the idea that Europe could maintain business as usual if China invaded Taiwan – is politically unrealistic, however. As Europe's security guarantor, the US could force the EU to choose sides. And even if the EU did not sanction China, US restrictions alone would harm China's economy, dampening demand in one of Europe's fastest growing export markets.

Taiwan is not amongst the top ten EU trading partners. But it produces more than 60 per cent of all semiconductors, including the most advanced computer chips found in everyday devices like smartphones. About 45 per cent

of the EU's chip imports come from China or Taiwan. A conflict would seriously disrupt these supply chains, depriving Europe's manufacturing industries of an indispensable input, and stifling Europe's access to digital technology. Although several European countries are subsidising their own local [chip-making facilities](#) and trying to mine [critical raw materials](#) locally to mitigate the risk of losing supplies, these efforts will take many years to become commercially viable.

The EU would therefore benefit if the Chinese economy was not walled off, or only in a limited way. That outcome is most likely if the EU successfully deters China from an invasion by aligning more closely with the US now.

The EU should learn from its experience with Russia. Deep trade ties did not dissuade Russia from invading Ukraine for two reasons. First, Putin bet that the EU did not have the political will or unity to impose far-reaching sanctions. Second, Putin wrongly thought that the EU would need cheap Russian energy supplies more than Russia would need European imports. China now understands that the EU is not afraid of imposing sanctions on large trade partners. To convince China not to invade Taiwan, however, European partners must persuade Beijing that the economic consequences of an invasion would hurt China more than the EU.

The EU's current approach is seemingly to try to minimise the costs of any China-Taiwan conflict for Europe, by pursuing its de-risking strategy. However its on-shoring and friend-shoring strategy faces many hurdles: it will take many years to achieve results, with higher costs and less efficiency. For example, the EU's efforts to mine or recycle more critical minerals in Europe involve environmental, technological and economic challenges that will take years to resolve. Europe also wants to conclude free trade agreements to increase imports of raw materials from countries other than China. But many of these agreements would be with countries such as Australia that have high production costs – which will not convince many European firms to diversify away from China.

So far, the EU has only targeted direct imports from China. Diversification risks making dependencies more hidden and indirect, however. For example, the EU might diversify sources of a particular import, such as refined rare earths, but that will not help if its new suppliers acquire their unrefined inputs from China. Although the EU quickly replaced Russian fossil fuels imports, China is far more embedded in European industrial value chains. De-risking effectively will prove far more complex and take

longer than the EU has acknowledged. Yet many experts expect that, if China invades Taiwan, it will do so within a few years.

To reduce the EU's dependency on China and Taiwan, EU institutions recently struck a [deal](#) for billions in subsidies to the chip sector to double Europe's global market share to 20 per cent by 2030. But the EU has only committed limited new funds to this goal, and analysts question whether the EU's ambitions are realistic. Even if EU production of chips increases, the Union will struggle to import enough inputs into the chip supply chain from outside China to keep pace: so the EU may become even more dependent on Beijing. Moreover, US and Asian countries are lavishing their own subsidies on local chip production, which means Europe will be competing in a subsidy race that not everyone can win.

Europe ought to consider an alternative approach: making the consequences of a conflict more painful for China, rather than less painful for Europe. In some cases, as China's economy has developed, it has started to replace high-value European manufactured products with domestic substitutes. A large proportion of EU exports to China are cars, for example: but that is likely to fall given the rocketing growth in China's electric vehicle production. European car-makers facilitated this development by relocating some production to China to serve the local market and to meet local content requirements, in order to qualify for Chinese subsidies. Europe's slow loss of complex, high-end industrial processes to China suggests Europe might benefit from moving somewhat closer to Washington's approach to deterring an invasion. This would include a mix of increasingly severe export controls, cutting government support for new European investment in China, and requiring government approval for such outgoing investments, thereby hindering China's technological advancement and keeping it more dependent on the West.

The US approach is not risk-free. It will encourage China to accelerate the indigenisation of technology. But China's business model relies heavily on Europe's large and wealthy consumer market, and Beijing also desperately wants a fragmented West. That means Beijing will be reluctant to retaliate against Europe so long as the EU remains even mildly more open to China than the US.

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As the European Commission becomes more political, it will need to embrace both the *Spitzenkandidaten* process and reform.

Nobody except for the European Parliament much likes the *Spitzenkandidaten* ('lead candidate') process, whereby the nominee of the largest political party in the incoming Parliament is supposed to become European Commission President. The CER has previously been [critical](#) of the process for two reasons: first, because it would not help to bring the EU closer to the citizens and to make it more democratic; and second, because a lead candidate system would over-politicise the Commission. But the Covid-19 pandemic and the war in Ukraine have called both conclusions into question.

The politicisation of the European institutions is not new. Jean-Claude Juncker's Commission (2014-19) was certainly [less technocratic](#) than its predecessors. But the crises Juncker had to face resulted in divisions both amongst the member-states and the EU institutions, limiting the power of the Commission (its inability to force member-states to take quotas of migrants is a case in point). In contrast, the emergencies of the Ursula von der Leyen era have brought about surprising unity. EU capitals have outsourced parts of their response to the pandemic and the war to Brussels. During both crises, traditional decision-making procedures were suspended in favour of emergency measures. This had the effect of sidelining the European Parliament and the Council of Ministers – the EU's usual co-legislators – in

favour of the [European Council](#) and, chiefly, the [Commission](#).

Today, the Commission, and especially its president, is enjoying a degree of independence rarely seen before. And this trend is set to continue, regardless of who leads it next. This is not because Commission presidents have suddenly become all-powerful figures, but rather because the global situation is forcing the Commission to become more involved in shaping the policies that respond to it. The EU's China [strategy](#) is a good example: after years of sitting on the fence, von der Leyen has come out in favour of '[de-risking](#)' from China, prompting capitals to start working on a clearer policy towards China. Putin's war on Ukraine is unlikely to end soon, and the Commission will have to continue playing a significant role on sanctions, energy, refugee protection and Ukraine's membership bid. Climate change, technology and trade will be other important areas where the Commission will often lead.

A more political Commission comes with a somewhat unexpected problem: enforcement. The Commission is the only EU institution that can bring governments before the European Court of Justice (ECJ) if they breach EU law. But, as EU integration professors Roger Daniel Kelemen and Tommaso Pavone [argue](#), a less technocratic Commission becomes "a more

legitimate law-maker (...), but at the cost of (being) a less credible law enforcer". The von der Leyen Commission has struggled to enforce rule of law provisions in the treaties, while keeping offending governments in the fold. The problem has been particularly [acute](#) since Russia's invasion of Ukraine. The next Commission will face similar challenges. If a [version](#) of the Commission's proposal to reform the Stability and Growth Pact ends up being adopted, senior officials worry that a member-state's ability to comply with fiscal rules will very much depend on how skilled it is in negotiating with the European Commission.

As the Commission becomes increasingly more political and embedded in EU citizens' day-to-day lives, it will face two separate but related challenges: first, how to make sure that Europeans get some say in who leads the Commission; and second, how to ensure that it continues to be able to enforce EU law, even as its political role grows.

As it stands, the *Spitzenkandidaten* process will not help with the first of those problems. Only half of those who can vote in the European Parliament elections [actually do so](#). And the elections are still too focused on [national matters](#). But there are a few changes that could help. The first would be for all European political parties to present one candidate who would campaign on clear-cut EU topics. In the past, only the largest groups in the Parliament have put forward a lead candidate. Both the Liberals and the Greens had reasons to be wary of a process that has traditionally mainly benefited the European People's Party and the Party of European Socialists. But this does not have to be the case any longer: the 2019 elections yielded the most fragmented European Parliament in history. And liberal prime ministers are in power in countries like Belgium, France and the Netherlands, while the Greens are in coalition in Germany. In many member-states, two-party systems have given way to complex coalition building, which incentivises smaller parties to run for elections in the hope of becoming king-makers. Current [polling projections](#) confirm this trend for the forthcoming European elections, too.

Second, European political parties should make the EU's shift from a technocratic to a political organisation work in their favour. Over the past three years, the Union has done previously unthinkable things, like procuring vaccines and funding weapons for Ukraine. It has also tried to shield EU citizens from economic hardship, by raising common debt, injecting money into the economy and jointly procuring gas. Von der Leyen is better known in the member-states (and the world) than most of her predecessors.

She has also expressed clear views on matters that European citizens [care about](#), like energy, climate change and the international situation. If she runs, other parties would have a chance to put forward candidates who could challenge some of her ideas, and even her handling of the pandemic and the war. Imagine a frugal candidate opposing joint debt, a farmer-friendly candidate arguing for less ambitious climate and energy policies, a dovish candidate favouring dialogue with Russia and China or a populist candidate outright opposed to supporting Ukraine. This would make for a *Spitzenkandidaten* process that looks more like a national political contest than a debate around ideas that few people outside the Brussels bubble care about.

Tensions between politics and enforcement within the European Commission will be more difficult to solve. Enforcement decisions cannot be made in a void. But the risk is that, in acquiring new political powers, the Commission will abandon its enforcement role altogether. Unlike in member-states, there is no other EU institution or body to which the Commission could outsource such powers (with the very limited exception of the European Public Prosecutor's Office, EPPO, the remit of which only covers crimes against EU financial interests). How can an increasingly politicised European Commission function both as an enforcer and a political master? One idea could be to create a new independent prosecutorial body or to expand the powers of the EPPO, but that would require lengthy negotiations and is unlikely to win the support of all member-states (Denmark, Ireland, Hungary, Poland and Sweden are not members of the EPPO). An easier way would be for the next Commission to reorganise its departments in a way that reflects the new situation. It could, for example, divide its directorates more clearly between those responsible for policy-making, drafting directives and so on; and those responsible for the executive functions of enforcing directives and regulations and launching infringement proceedings. Vice Presidents should also be more accountable to both the European Parliament and the European Council – by, for example joining meetings of the latter when matters under their supervision are discussed.

The pandemic and the war have made the European Union more powerful. EU governance should reform accordingly.

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# 25 years on...

by Charles Grant

This 150<sup>th</sup> edition of the bulletin appears 25 years after the first. It prompts me to recall the birth of the CER in 1998.

Both Nick Butler, then a senior executive with BP, and David Miliband, then a policy adviser to opposition leader Tony Blair, played a crucial role. As they explained in their recent articles in [bulletin 148](#), they had a chat during a dull moment of the British-German Königswinter conference in 1994. They agreed that Britain needed a new think-tank to work on Europe. The rationale was clear: a Blair government would want a closer relationship with the EU but needed analysis and ideas. None of the existing think-tanks was particularly well-placed to provide them.

Nick and David convened a series of meetings to plan the think-tank. They invited me, then defence editor of *The Economist* and its former Brussels correspondent. Ben Hall, who had worked for shadow foreign secretary Robin Cook, soon became the CER's first employee and played an essential role. Though the CER had no office, it published its first four pamphlets in 1996, unveiling them at a launch party at Price Waterhouse.

One pamphlet was a memorable short essay by Ralf Dahrendorf, a British-German peer and former European commissioner. He set out ten principles for European renewal, concluding: "A Europe which pretends to be a nation writ large, even a superpower, is in fact a monstrous construction rather than an ideal. European co-

operation among democracies is a sensible way of dealing with a number of issues which elude even large nation-states and cannot yet be done globally. It is no more, but also no less."

Dahrendorf was an active member of our advisory board in the early days – and was often cussed and critical of what we did. So was John Gray, who is now one of British intellectual life's leading critics of liberalism and of Europe, but in those days was a pro-EU Blairite. The most important board member was David Simon, chairman of BP when the CER was conceived. He persuaded friends in the business world to stump up the cash that allowed us to start doing things.

The donkey work of planning and organising the think-tank fell on a group of young men and women who were broadly New Labour, most of whom got jobs as special advisers in Blair's first government in 1997: Wendy Alexander (who went to Scottish secretary Donald Dewar), David Clark (who went to foreign secretary Robin Cook), Julian Eccles (who went to culture secretary Chris Smith) and of course David Miliband (who ran Blair's policy unit). *Financial Times* journalist Stephanie Flanders also lent a hand.

After the 1997 election, more work was needed before we could establish a proper office. Two



people were especially helpful: Maurice Fraser, who had advised Conservative foreign secretary Douglas Hurd and later ran the European Institute at the London School of Economics (he died in 2016), and Liam Byrne, who became a Labour minister and remains an MP.

In January 1998 I left *The Economist* to join Ben Hall in our new office in Tufton Street. Soon afterwards, we launched the bulletin, as a vehicle for shorter pieces. In 2006, writing in a special [50<sup>th</sup> edition](#) of the bulletin, I highlighted some of the outstanding contributions we had had from guest authors. Jacques Delors, for example, had written a piece criticising the drafting of a European constitution, since, he said, constitutions belonged to nation-states. “My vision of an enlarged Europe is that, at the start, it should consist of both a geopolitical entity bringing together a wider Europe – ‘the Union’ – and an *avant-garde* that is overtly organised into a federation of nation-states.” Rather Macronian.

In our early years we were in many respects a New Labour think tank, but we soon worked out we would have more influence as a cross-party institution. We have happily engaged with serious politicians of all persuasions, including all the Conservative governments since 2010. This was not always easy during Boris Johnson’s government, but we still found Conservative ministers willing to speak on our platforms.

Ever since its foundation the CER has had two missions – to come up with ideas and policies for making the EU more effective; and to improve the quality of the EU-UK relationship. Much as we regret the decision of the British to leave the EU in 2016, we are confident that our twin missions remain as pertinent as ever. Brexit did make the first mission slightly more difficult in some quarters, which is why we opened offices in Brussels and Berlin. We have not found it difficult to demonstrate that we are a European think-tank: the proportion of our researchers that are non-British has seldom dipped below 50 per cent.

Not only our missions have remained constant, but also our style. We are a serious, sober, think-tank that believes in evidence-based policy-making. The CER is certainly media-friendly, which is why we are often quoted, but we are not a flashy organisation. Our prescriptions – and we make lots of them – are within the bounds of practical politics. We want to be useful to policy-makers and are less academic than some think-tanks. Our small size – the staff has never exceeded 13 or 14 – has fostered a

culture of teamwork (we avoid silos: foreign policy experts edit pieces by economists, and vice versa).

We have maintained output of extremely high quality for 25 years because our researchers – supported by a superb admin team – have been brilliant. Here are the names of our previous full-time researchers, and where they ended up. Alex Ashbourne is a defence consultant; Katinka Barysch is director of political relations at Allianz; Sophia Besch is at the Carnegie Endowment in Washington DC; Hugo Brady worked for European Council President Donald Tusk and is now at the International Centre for Migration Policy Development in Vienna; Edward Bannerman worked in several EU cabinets and is now with the European Bank for Reconstruction and Development; Edward Burke is a lecturer at University College Dublin; Steven Everts worked in several EU cabinets and is now in the External Action Service; Agata Gostyńska-Jakubowska is head of government affairs for Central and Eastern Europe at Apple; Heather Grabbe worked in an EU cabinet and then ran the Open Society European Policy Institute; Ben Hall is Europe editor of the *Financial Times*; Daniel Keohane is at the Brexit Institute, Dublin City University; Rem Korteweg is at the Clingendael Institute; Bobo Lo is an independent analyst; Christian Odendahl is European economics editor of *The Economist*; Beth Oppenheim is at the Tony Blair Institute in Israel; Mark Leonard runs the European Council on Foreign Relations; Sam Lowe is a partner at Flint Global; Alasdair Murray is head of corporate affairs at KPMG; Simon Tilford is a director of the Oracle Partnership; Adam Townsend is a corporate lawyer; Kitty Ussher was an MP and minister and is now chief economist at the Institute of Directors; Tomáš Valášek became Slovakia’s ambassador to NATO and is now a Slovak MP; and Aurore Wanlin is director of corporate communications at Edelman.

Let us also remember three gifted colleagues who died very young: Clara Marina O’Donnell, Stephen Tindale and Philip Whyte.

If the EU evolves in such a way that it no longer needs reform, and the UK-EU relationship reaches a stable and happy equilibrium, I shall be the first to suggest winding up the CER. But I suspect the CER will still be in business in 25 years time.

**Charles Grant**  
Director, CER [@CER\\_Grant](#)

## CER in the press

### The Economist

22<sup>nd</sup> May

"Whether the EU will manage to meet its ambitious climate goals will now depend on member states' willingness to deliver on the plans and to abstain from watering down any legislation that does not sit well with their voters," says Elisabetta Cornago of the CER in Brussels.

### The New York Times

21<sup>st</sup> May

Europe is "less on top of Greece for doing pushbacks and all that sort of thing," said Camino Mortera-Martinez, who heads the Brussels office for the CER. The latitude given Greece, she said, was in part recognition that the country had lived through a decade of brutal austerity. But it also reflected that Europe as a whole is "basically unable to help" Greece and other nations at the front line of the migration crisis, and therefore lets "these governments do what they do."

### Bloomberg

20<sup>th</sup> May

"Immigration pretty much automatically adds to GDP because there are more people in the country working and consuming,"

said John Springford, deputy director of the CER. "We have some good evidence that immigration actually helps to grease the wheels of the labor market a bit, and allows people to hand off lower-productivity tasks to other workers and concentrate on things which they were most productive at."

### Le Figaro

11<sup>th</sup> May

"France's budgetary situation weakens its position as the second pillar of stability in the eurozone alongside Germany, in the face of major challenges such as the war in Ukraine, defence or climate change. There is real concern," notes Sander Tordoir, senior economist at the CER in Berlin.

### Ekathimerini

14<sup>th</sup> May

"If Turkey's current president, Recep Tayyip Erdoğan, wins, the EU will continue its policy of transactional co-operation with Turkey and crisis management when they break out. Erdoğan's approach to the war being waged in Ukraine will be a key variable and potential source of tension, particularly if Turkey does

not lift its veto on Sweden's NATO membership," said Luigi Scazzieri of the CER.

### The Guardian

10<sup>th</sup> May

"If the EU moves first and has sensible standards other countries will start with the EU rules when designing their own regulation," said Zach Meyers, senior research fellow at the CER.

### Handelsblatt

10<sup>th</sup> May

Baerbock's visit is only the prelude to a new harmony offensive with which Macron and Scholz want to revive German-French relations, which have been in crisis for some time. "You can tell that things are bad when Paris and Berlin emphasize symbolism," says Charles Grant, director of the CER think-tank.

### Financial Times

6<sup>th</sup> May

In his paper for the CER, Luigi Scazzieri outlines the possible consequences of an Erdoğan victory: louder calls in Europe to formally end Turkey's EU accession process; a rise in tensions between Ankara and Athens and Nicosia, which might lead to pressure for more EU economic sanctions on Turkey; strains with the US

and Europe over Turkey's relations with Russia, particularly in the context of the war in Ukraine; and more difficulties with the west if Erdoğan maintains his veto on Sweden's NATO entry.

### The Economist

4<sup>th</sup> May

"The risk of the current discussion on fiscal rules is that we lose sight of the bigger picture," says Sander Tordoir of the CER. The EU is heading for a spending squeeze that requires not rule-tweaking, but a new fiscal settlement.

### The Times

2<sup>nd</sup> May

"The UK is getting way ahead of the European Commission on mergers," Zach Meyers of the CER says.

### Voice of America

21<sup>st</sup> April

"The ban on imports of Ukrainian grain by some countries in Europe could play into Moscow's hands, Ian Bond of the CER said. "It seems to me that this increases the chances that Russia will see this as a pressure point and will try to use it as a way of saying, 'Well, we're not going to renew the grain deal unless you agree to completely unacceptable conditions.'"

## Recent events

### 25 May

Lunch on 'The impact of the war in Ukraine on NATO', Brussels  
 Speaker: Julianne Smith

### 23 May

Breakfast on 'Reflections on the Northern Ireland protocol and the UK's relationship

with the EU', London  
 Speaker: Chris Heaton-Harris

### 27 April

CER/AIG Geopolitical Risk Series:  
 Webinar on 'Xi Jinping's China: What next?'  
 Speakers: Jörn Beißert, Bonny Lin,

Kristin Shi-Kupfer and Friedolin Strack

### 25 April

Dinner on 'EU competition policy, industrial strategy and the global economy', London  
 Speaker: Olivier Guersent

For further information please visit

**www.cer.eu**