US-China Strategic Economic Competition: Impact on EU-China Relations

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1. INTRODUCTION

As the European Union was recovering from the deepest economic crisis since the Euro was created, a number of new challenges popped up. First and foremost, Brexit since June 2016 and a growing number of anti-European and/or populist governments with the most recent – and probably most relevant case – being Italy. Beyond those internal problems, another external shock hit the EU in 2018, namely, the trade war between the US and China. The US-led trade protectionism against China affected the European Union in several ways. First and foremost, it puts multilateralism in trade relations at risk and, in particular, the good functioning of the World Trade Organisation (WTO) (Jean, Martin, and Sapir, 2018). Second, it opened the door to additional trade protectionism which could possibly impact the EU as it sits on the largest trade surplus in the world. Third, trade measures taken by the US against China as well as China's retaliation have indirect consequences on Europe. These can be positive for some sectors and European exporters have gained a comparative advantage against US exporters in China markets for the US goods on which import tariffs have been imposed and that Europe can produce (Wolff, 2018). Conversely, European exporters have an advantage in the US market compared to Chinese exports for those sectors targeted by the US with tariffs. However, this positive scenario gets blurred when one thinks of the complexities of the global value chain which can lead to increases in European costs of production due to third countries' import tariffs as long as they lie within Europe's production chain (Chiacchio, 2018). This is, no doubt, the case of China.

Given the above complexities, it is important to analyse in detail what has happened so far in the US-China trade war and beyond trade as this article will hold the view that trade is just one of the facets of a much more structural economic confrontation between China and the US. Second, we move to analyse the EU's potential gains on the basis that the trade measures taken by the US and China on each other can help us to focus on Europe's potential gains, at least at a sectoral level. Finally, there will be a review of Europe's strategic options in a world that tends to be increasingly divided into two blocs (China and the US).

The paper is divided into 5 sections. The first section is to introduce the background of the US-China trade war. The second section is to provide a review of US-China trade protectionism and the impact of the trade war on China and the US. The third section is to show a sectoral analysis of trade measures taken by China and the US. The fourth section illustrates EU's first-best strategy regarding the US-China trade war. The fifth section discusses how the EU should behave in the US-China trade war.

2. THE CURRENT STATUS OF THE US-LED TRADE WAR

The trade negotiation between China and the US is a key factor influencing market sentiment. First of all, it is important to realise that the trade war has evolved into a more complex reality, namely the strategic competition between the two largest economies in the world. Within that context, US expectations regarding China seem to be gearing towards two fronts: increasing Chinese imports from the US (not necessarily a market measure) and improving market access for US companies in China. For the latter, a better legal framework for protecting intellectual property rights and discouraging forced technology transfers is the key. More generally, a foreign investment law reform is an inevitable way for China to improve the market environment for foreign firms.

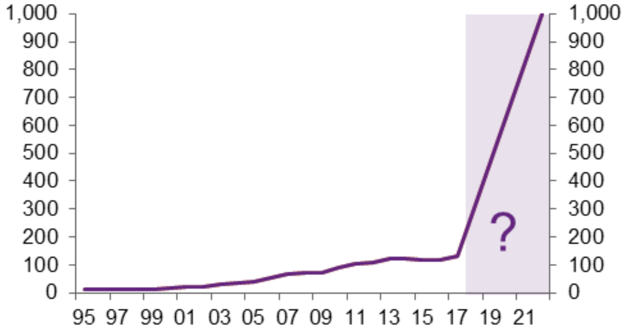
Under pressure exerted by the US, China is moving on these fronts. While achieving such measures could be beneficial, especially for the US, it is not necessarily the best outcome in all dimensions. In particular, targeted imports will create trade diversion for China, thereby reducing China's imports from the US' main competitors, Europe and Japan. Also, forcing better market access will not be sufficient to solve China's key economic characteristic, i.e., state capitalism.

As such, the true target of the US seems to be not only turning China into a market economy, but rather pushing it into a stream of imports from the US and forcing it to offer better market access to foreign companies. However, even such agreements cannot be fully achieved in a single meeting because of the complex reality. The most likely outcome of this round of negotiation is to reach consensus on some specific measures. That said, the "partial" deal should still be perceived positively by market participants because it allows both parties to freeze additional import tariffs which had been announced earlier.

Down the road, China's increasing wages and its quest to bypass the middle-income trap leave no option for China but to continue to move up the technology ladder. The movement will only increase the US' containment forces, especially as far as technology is concerned. The announcement of possible progress is at most a "partial" deal, which could be well received in the market but is only a temporary solution which masks the structural competition between the two economies.

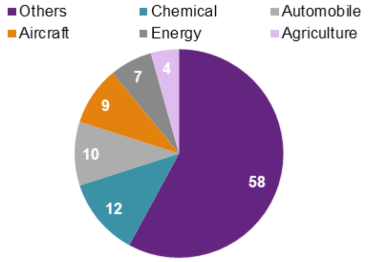
All in all, for the ongoing negotiation, China needs to accommodate the requests to calm the US, but it cannot give up its strategy of moving up the technology ladder to escape the middle-income trap.

Chart 1
US Export to China (USD bn)



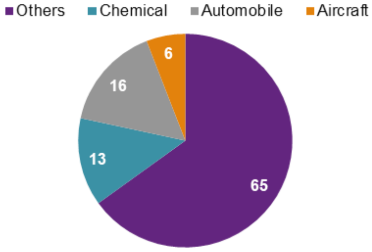
Source: Natixis, UNCTAD

Chart 2
China's import from US
Breakdown by sector (%)



Source: Natixis, UNCTAD, UNCOMTRADE

Chart 3
China's import from EU
Breakdown by sector (%)



Source: Natixis, UNCTAD, UNCOMTRADE

3. AN ACCOUNT OF US-CHINA TRADE PROTECTIONISM

From seemingly untargeted measures announced in early February 2018 for solar panels and washing machines, the US has moved to increasingly targeted action against China. The most obvious case in point was the announcement of 25% additional import duties to be applied to USD 50 billion equivalents of imported goods from China on the basis of China's infringement of intellectual property rights (Garcia Herrero, 2018a). More importantly, about two thirds of those import tariffs have been applied since 6 July. The US' speedy introduction of the announced import tariffs, without allowing for much time to negotiate a deal between China and the US, shows the US resolve to move away from the status quo in terms of the functioning of the global trading system, at least as far as China is concerned. On that basis, China had no choice but to retaliate with equivalent import tariffs on US goods.

Since then, the list of Chinese imports that the US is aiming at increasing tariffs on has expanded to an additional USD 200 billion. Thanks to a three-month truce reached recently at the side-lines of the G-20 summit, the additional USD 200 billion goods from China will not be confronted with a 25% import tariffs yet but it looks increasingly clear that this is just a truce to buy time for both sides and that the confrontation is escalating. The recent arrest of Huawei's CFO because of a potential breach of sanctions against Iran is the proof of the pudding of how far the US is ready to go in weaponizing its current hegemonic position as rule setter.

Going back to the trade war, China's ability to retaliate on trade is obviously more limited as it does not import enough goods from the US to match the announced additional USD 200 billion in import tariffs from the US, which explains why China's second batch of retaliatory measures have been more moderate, at least in size (USD 60 billion). Also the latter have been put on hold thanks to the recently agreed three-month truce.

The market reaction so far seems to have been more negative for China than the US, at least as far as the stock market is concerned, which has lost more than 20% in value year to date. Furthermore, the RMB has depreciated quite substantially since the beginning of the trade war until recently, helped by the recently announced truce between the US and China. One may wonder whether the market is overreacting to the potential consequences of such a trade war on China or, perhaps, underestimating the impact on the US. So far, European markets seem to have remained relatively more insulated from the US-China trade war except when the US pointed towards protectionist measures against Europe directly, as was the case when the tariffs on EU steel and aluminium were raised in spring 2018 and threats over increasing import tariffs on autos and auto parts were made in early summer 2018. Moving on to the potential economic impact of the trade war, there have been attempts to estimate the direct impact of tariffs on trade and, thereby, on growth. For example, the International Monetary Fund (IMF) in its latest World Economic Outlook has estimated that the Chinese economy would grow 1.6% point less in 2019 and the US economy would grow 0.9% point less in 2019 if the trade war were to be maintained in 2019. Also, the Euro area's growth rate would be shelved by 0.4% in that scenario. The World Bank, in contrast, has a much more benign scenario in its latest global economic prospects, as it has estimated that the Chinese economy will only grow 0.2% point less in 2019 and the US economy will grow 0.2% point less in 2019. In the same vein, estimates of price and income elasticities of Chinese exports into the US by Garcia Herrero (2018b) point to a relatively limited value of China's total exports affected by tariffs. Even if the USD 200 billion Chinese goods were to be confronted by full 25% tariffs, the overall impact on Chinese trade would be limited to only 3% of China's exports and only 1.3% of the US' exports.

Overall, the reason for this relatively limited economic impact, especially when compared with the very negative market reaction, especially for China, is that such exercises only take into account the direct effects of tariffs on trade and not indirect effects on investment through a worsening of market sentiment, among many other channels. The impact on expectations and, thereby, future investment, is probably behind the market fear, especially in China but also in the US and, to a lesser extent, Europe.

The issue is that the market may be realising that the risk is not only protectionism but much more than that as the US' ultimate goal is to try to contain China. In fact, investors both in China and abroad are starting to worry that their investments may possibly be completely blocked by the US or indirectly affected by the worsened relationship between China and the US (Garcia Herrero and Xu, 2018). Moreover, the multilateral trade order maintained by the US is likely to be massively transformed. If that happens, the world will have to return to a much less free system for goods and services flow. It is due to these increasing uncertainties that market investors' sentiments have become more and more negative.

One way to go about analysing the potential impact of the ongoing trade war might be to look in more detail at the measures taken so far and analyse their rationale so as to draw conclusions about their potential consequences down the road.

4. A DEEPER ANALYSIS OF THE TRADE MEASURES TAKEN BY THE US AND CHINA

The analysis of the sectoral composition of the goods targeted by the US administration would support the view regarding relevant structural changes to happen in the global economy due to the trade war. The first round of the US tariffs (USD 50 billion) was aimed at China's high-end exports, with a view to containing China's technological advance, with 7% on very high technology products and 55% on high technology products (Garcia Herrero, 2018c). Some of the products included in the US tariffs list have not been exported to the US yet, such as aircraft and aerospace or arms and ammunition, so the US' true intention of the tariffs is not to reduce the trade deficit with China, but to contain China's move up the technology ladder. By including products that do not contribute at all to the US' bilateral deficit with China, one could argue that the US is revealing its preferences, at least indirectly, which are to contain China in what it wants to become, namely a technological power that competes with the US in high-end products.

Very interestingly, China appears to have realised quite quickly the US intention as it has rapidly modified its own retaliation list from a more balanced one which included high-end imports from the US (including aircraft and aerospace) to one more focused on low-end products, such as agriculture (especially soy) and energy. Such a strategy makes sense as imposing tariffs on high-end products which China does not yet produce or cannot be sourced from anywhere else would only hurt China. This is because it would only increase the price of products needed for China to achieve its ultimate objective, namely, to move up the value chain ladder.

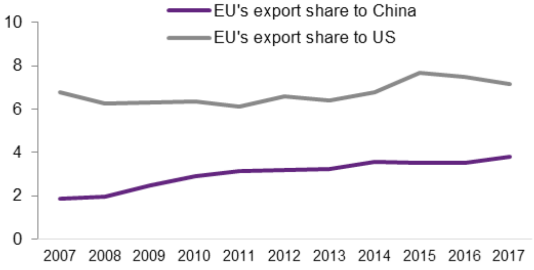
Moving on to the second set of import duties announced by the US, namely that of USD 200 billion to be imposed by 30 August, the products composition seems to be very different. In fact, low-end products dominate but, interestingly, very few of them are final – especially consumer – products (with only 22% of the total) but rather are intermediate products. One could interpret this second wave of import tariffs as a way to re-shore the production of intermediate goods back to the US (or at least to a third country which is not China) and reduce China's role in the global value chain. This interpretation of the second round of tariffs could have tangible implications for third countries which are now part of the value chain and have better economic relations with the US (even a free trade agreement which insulates them from increases in US import tariffs across the board). This is the case with Vietnam as well as Mexico (if NAFTA is finally renewed). But the US has silently removed some key products which would be expensive to substitute in terms of increase in prices for the final consumer (such as white goods for which China has become the largest supplier by far).

For this second round of tariffs, China's retaliation is much smaller, only USD 60 billion, due to the limitation of the total volume of China imports from the US. Yet, it is already a large bulk of the total retaliation list China can further extend. In this round of retaliation, all low, medium and high technology stuff are included, which shows a determined stance by the Chinese authorities that they will not retreat from the US threat. Also, more high-technology products were included as China's imports from the US are limited.

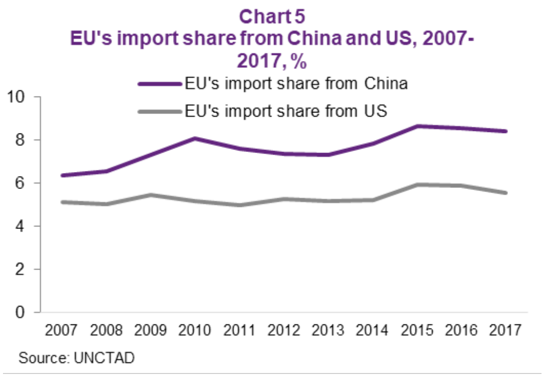
5. WHAT IS THE IMPACT ON EUROPE?

Potential European gains or losses arising from the US-led trade war on China will very much depend on whether Europe remains neutral on the US-China trade war instead of following the US' lead by imposing import tariffs on China. If the EU is forced to pick the US side and imposes its own import tariffs on China, China will probably also retaliate against EU companies. It should also be noted, though, that the potential gains to be made are bigger in the US (beyond the already larger export revenues), largely due to more tariffs imposed from the US side. In other words, beyond Europe's historical alliance with the US, which will keep the EU closer to the US than they would ever be with China, the EU also fears losing the US market even more than that of China as its export share to the US is larger than China (Chart 4) while China remains more relevant for EU imports (Chart 5). The fact that Europe, an overall net exporter, continues to maintain a bilateral trade deficit with China does not help (Chart 6). Obviously, a neutral stance as regards China is the best of all situations, with some clear winners among European export sectors, but the US clearly comes first in the EU's interests even if you only focus on trade gains.

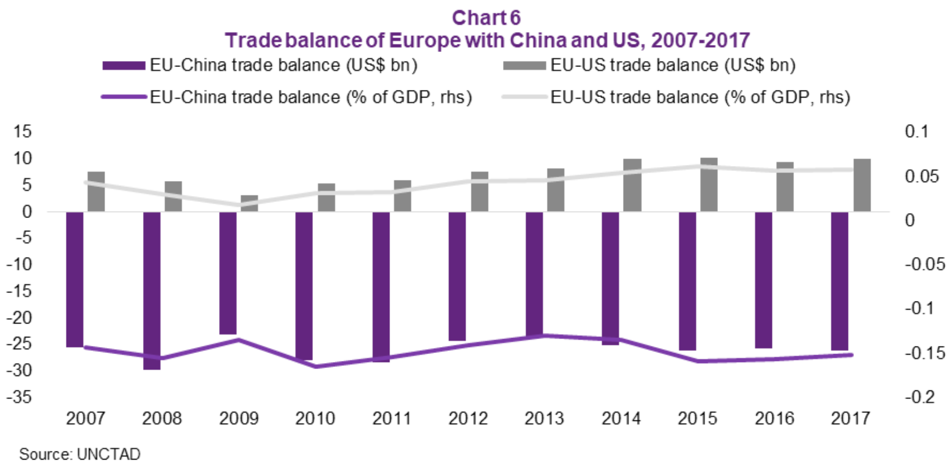
Chart 4
EU's export share to China and US, 2007-2017, %



Source: UNCTAD



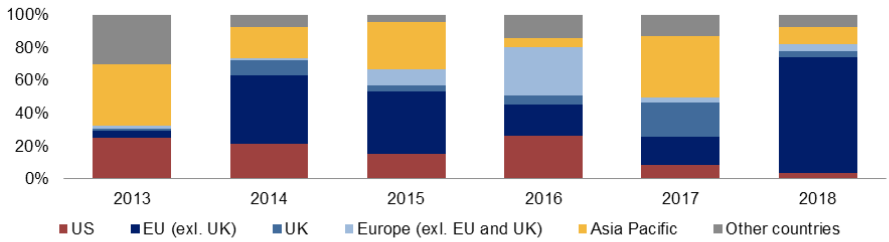
All in all, our analysis shows US-China trade frictions are here to stay in so far as they are a response to a fight for hegemony in the global economy. The US wants to contain China's future – which basically implies direct competition with Chinese products in third markets. In that regard, Europe, being export oriented and with a similar economic structure, can benefit by substituting some of their exports to China. This, however, requires that there be no retaliation from the US towards Europe. Otherwise, it will be extremely difficult for the EU to keep a neutral stance on the trade war.



Beyond trade an increasingly important consequence of the US strategic competition with China is that the latter is turning to Europe to acquire relevant companies to move up the technology ladder. More specifically, in 2011, China's outward foreign direct investment (FDI) (including that from Hong Kong) accounted for only 1 percent of EU total inward FDI, whereas China took 3.5 percent of the EU's outward

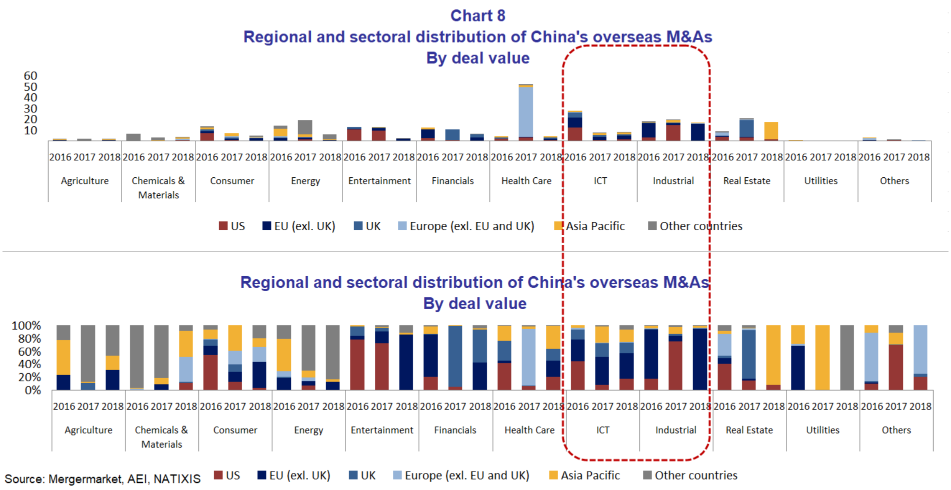
FDI. Given the size of the Chinese economy in the world already in 2011, this can be considered relatively modest. The situation today is very different. Chart 7 shows that Europe, especially the EU-27, has become, by far, the most attractive destination for China's overseas acquisitions, accounting for 70% of the total in terms of deal value, particularly in the industrial and information and communications technology (ICT) sectors where China has been eager to cooperate to climb up the technology ladder (Chart 8). Because the US has closed its door to China on the basis of "national security concerns", the EU is now the only place that is easier for China to access in buying foreign companies.

Chart 7
Destination of the overseas completed M&A
The percentage by deal value



Source: Mergermarket, AEI, NATIXIS

Chart 8

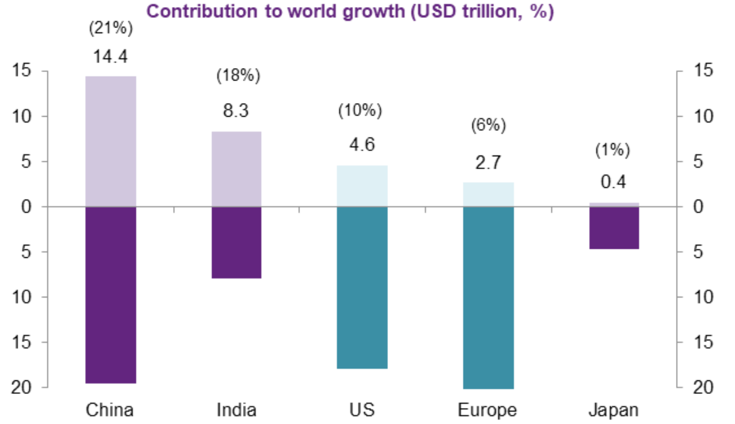


Source: Mergermarket, AEI, NATIXIS

6. OPTIONS FOR EUROPE IN LIGHT OF INCREASING ECONOMIC COMPETITION BETWEEN CHINA AND THE US

What the US-China trade war has brought about is not only short-term trade tensions, but more importantly, a systematic shift in the trade order which has supported the world's development for the past century. Undoubtedly, the US and China will be the most influential bloc in the 21st century, and their conflict is doomed to be long lasting. While the two countries may find some temporary solution to the current tariffs dispute, their conflicts are intrinsically embedded in the competitive stance, which could only be exacerbated in the future. This is all the more natural when we realise that China's economy is already as large as that of the US (at least in purchasing power terms and soon in USD terms) but, most importantly, will contribute more than three times that of the US to the global economy in the next 10 years (Chart 9). In other words, although the US is a more important market for Europe today, this will soon no longer be the case, based on the positive growth differential between the US and China, which continues to be very large.

Chart 9
Contribution to world growth (USD trillion, %)



Source: Natixis

The global influence of the US-China cold war will be persistent. At this turning point, as the world's only figure that can balance the power between the US and China, the EU has to decide how to respond to the trade war. There are several options under current discussion.

Safeguard multilateralism?

The EU has long called for economic multilateralism and is pushing for the reform of the WTO to adapt to China's sheer size without it having become a market economy. In fact, one could argue that one of the key areas of contention from the US side is indeed China's different economic model while still being part of a free trade world. The European response to this reality is to keep, if not enhance, multilateralism, by reforming existing institutions, especially the WTO, so as to impose market practices on all members in order to protect fair trade (Demertzis, 2018).[1] This really means that the WTO will need to address the issue of the large role of state-owned enterprises (SOEs) in the production of goods and services and the pervasive role of subsidies in production. This would bring the WTO close to the US concerns over China's unfair practices in international trade.

While the EU may easily find common ground on the key issues with the US (only if the current US administration were to engage in such a reform, which is not the case now), it could be hard to achieve the requested reforms in China. In fact, the role of SOEs is considered key in China's model of socialism with Chinese characteristics and, thus, they are impossible to dismantle in the foreseeable future. The Chinese will argue that the role of SOEs remains moderate[2] and, thus, should not be an issue for WTO reform. The Chinese have also borrowed the concept of competitive neutrality from the Organisation for Economic Co-operation and Development (OECD) and have argued that they are increasingly close to applying competitive neutrality among companies operating in China. Garcia and Xu (2017) hold a very different view on the role of SOEs in the Chinese economy both because of their more pervasive influence but, more importantly, because of their very different nature compared to other SOEs in the world. In fact, the key reason for their unequal footing with the rest of companies operating in China, including private Chinese companies, is their preferential access to market in many sectors as well as their special connection with China's long-standing ruling party, namely the Communist Party.

That said, the EU will also find the US difficult to cooperate with in the reform of the WTO. Since his arrival to power, Trump has pushed "America first" policies and certainly not policies in support of multilateralism. In fact, the tariffs measures taken by the US based on "security" reasons while bypassing the WTO's multilateral

1 For more details as to how Europe can defend multilateralism in the world and what the options are for Europe, please see, Jean, S., Martin, P., and Sapir, A. (2018) and Wolff G. (2018).

2 According to China's National Bureau of Statistics, in 2015, SOEs accounted for 38.8 percent of total assets for industrial enterprises above scale.

settlement mechanisms is a clear sign that the US may overthrow the multilateral value based on its own interests. As such, while the US seems to share more of the market and democratic values with the EU, it does not seem ready to fully conform to the EU's proposal for a WTO reform so as to preserve multilateralism.

Under such circumstances, it does not seem very credible for the EU to continue to push the agenda of multilateralism without the support of the US and China. On the other hand, though, it looks extremely dangerous for the EU not to do so as it is no longer a superpower, nor does it intend to be one. All in all, while continuing to make efforts to preserve multilateralism, Europe may need to explore other responses to the current standoff between China and the US, aware of the increasingly slim chance that multilateralism becomes the driving force again.

Enhancing Europe's Reliance on the Transatlantic Alliance?

Another potential option for Europe is to maintain the status quo while reinforcing it on the basis of an increasing economic confrontation between the US and China. In other words, the EU may also choose to lean completely on the US. The question is whether it is wise to do so in the current environment with clear changes in the US attitude towards multilateralism. This is all the more disappointing in so far as it was the US which had pushed for such a system, as a way to create a safe environment for its allies and eventually to enable it to engage the rest of the world after the collapse of the Soviet Union.

The current US administration has made it very clear that multilateralism and open trade is something of the past. The gunfire that the US has triggered is not only against China but against many other countries, including the EU. Just in 2018, the US has already threatened tariffs on steel, aluminium, and cars on the EU. It also criticised the EU for its large trade surplus against the US. Also, the US has criticised the EU for not fulfilling its economic responsibility on military spending as members of the North Atlantic Treaty Organisation (NATO). As such, the EU alliance with the US will be more costly for the EU than it has ever been as the US is not happy with the current distribution of costs and benefits of the Transatlantic Alliance.

More importantly, because the US has chosen a non-market bilateral way to deal with China as well as other issues, the EU's complete support for the US will mean that it has to give up on its rule-based approach to problem solving and, thereby, its principles. This is obviously very costly for the EU as its own internal market is based on a strong rule-based system as well as for the world since the EU is the bastion of multilateralism. The case of the reform of the World Trade

Organisation is a clear case in point since the EU is really holding on to it and would probably not manage to do so if pushed towards a relation of clear dependence on the US.

There is another practical reason which restricts the EU from leaning on the US completely. The EU is not a single country but a group of 28 (soon probably 27) countries which have different views about the US and also about China. In fact, while it may be easier for Western Europe to unite against China, Eastern Europe, but also Greece and Portugal, and recently perhaps even Italy, may express opposing views as to a strategic alliance with the US which requires leaving China aside. In fact, the recent effort of the EU to establish an EU-level investment screening system resembling the US' famous Committee on Foreign Investment in the United States (CFIUS) has been vetted to such an extent by some EU members that its final version is really very limited in scope and hardly a threat for China. China has also created a platform with Eastern European and Balkan countries, the so-called 16+1, since all of these countries are part of China's Belt and Road Initiative (BRI). Many of these countries expect to ease their financial concerns through investment from China as well as to reduce their dependence on Brussels. This, in itself, poses problems for the EU and might actually push it even closer to the US, notwithstanding the costs.

Strengthening Cooperation with China

Strengthening cooperation with China is also a practical – albeit unlikely – choice for the EU in so far as its current strategic ally, the US, is moving away from multilateralism, thereby harming EU interests. In fact, not only is China's economy of a similar size to the US already today but its contribution to global growth will be much bigger in the future, as previously shown. This means that opportunities in the medium term should be bigger in China but under a very important hypothesis: market access.

This is why most of the discussion as to whether Europe should rebalance its economic partnership towards China, at least partially, boils down to improving European companies' market access in China. Within that context, the EU had started negotiating a bilateral investment agreement (BIT) with China at a time when the economic relations still had a positive perception from the European side but things have changed quite dramatically since then. In fact, the 12th round of BIT negotiations has been without an agreement. The key stumbling block is indeed market access for European companies in China and reciprocity, which is of course related to the perceived lack of market access.

Beyond market access, EU authorities are concerned about potential discrimination against EU investors operating in China, including explicit or implicit preferential subsidies for certain enterprises. Such discrimination may also be a factor for Chinese companies operating in Europe. While market access is a more general issue, potential discrimination by means of implicit or explicit subsidies has linkages to the role played by Chinese SOEs. This is not only true for the Chinese economy, but also for Chinese investments in Europe because a good part of it (most of it until very recently) originates from SOEs.

In China, SOEs have a much wider scope as they originate from the planned economy era when they dominated all sectors (either SOEs or collectively owned companies). Most Chinese SOEs, even now, are not established on the basis of correcting market failure, but more to carry out government objectives. Chinese SOEs are bigger, more pervasive, and more dominant than their EU counterparts, and, more importantly, exist in nearly every key sector in Chinese society. Against this backdrop, the Chinese government has created a special favourable environment for the SOEs. This actually triggered the concerns over their unfair competition in the international market and is one of the key barriers confronting China's building of an economic alliance with the EU. The hope for an EU-China BIT is that it should foster investments on both sides, but the reality is that, at this current juncture, Chinese investment into the EU is ballooning while EU investment into China is slowing down and is already smaller than that of China's investment into the EU.

All in all, given the increasingly difficult relations with the US, a certain degree of rebalancing towards China should be explored by the EU. However, the key stumbling block will continue to be China's state capitalism and the lack of market access for foreign companies. For the specific case of state-owned enterprises, preferential market access in China, rather than ownership of SOEs, should be the key consideration for European policy makers when evaluating the undue advantage enjoyed by Chinese corporates. This is because private companies with ties to the Chinese government might also benefit from preferential market access. The recent case of Huawei shows how much the Chinese leadership may support key private companies, especially if they belong to strategic sectors.

More generally, the highest priority issue that an EU-China BIT should pursue is market liberalisation, so that any market access granted through the BIT puts European companies on an equal footing to their Chinese competitors (even with SOEs). This obviously requires, at least, reciprocity (García Herrero and Xu, 2017). In fact, market liberalisation is important not only for foreign companies but also for Chinese private companies so that gains are also shared with China.

While engaging with China in its liberalisation and opening up, the EU cannot remain fully open to China's acquisitions of technology and the competition of Chinese state-supported companies in the single market. Europe has just announced a stricter framework for the screening of foreign investment (mainly directed at Chinese companies). Still, three key instruments might be used, with some reinterpretation of the EU Treaty, namely competition, dispute resolution and state aid policy. The first one does not require explanation nor does state aid policy, with the caveat that it cannot yet be applied to non-Member States. As for dispute resolution, identifying unfair behaviour by a firm can be easier after a firm reveals its status by operating in the EU market. An appropriate dispute settlement mechanism can protect both European and Chinese corporates. Among the different options, an investor-state dispute settlement system (ISDS) seems to be favoured internationally, but would need to be revised so that governments (either China or EU governments) do not fall prey to corporates suing them without clear justification. Furthermore, in the Chinese case, the very close links between corporates and the Chinese government (especially when operating abroad) could make the ISDS a double-edged sword for the EU, because in certain cases China could, for its own purposes, support its enterprises in suing EU companies. In addition, the implementation of the ISDS might be difficult in China where experience with investor-state arbitration is rather limited and there is very low probability that the Chinese government will enforce foreign court decisions. A revision of the ISDS is thus warranted so as to balance the interests of the parties in the BIT negotiation.

As such, we can see that Chinese internal reform is the key for the EU to pursue a better alliance relationship with China. The priority issue that EU and China need to pursue is market liberalisation, so that any market access granted through the BIT puts European companies on an equal footing to their Chinese competitors (even with SOEs). This obviously requires, at least, reciprocity. Yet, there is still a long way to go in this direction.

7. CONCLUSIONS

This paper reviews the impact of the US-led trade war against China and its immediate consequences, not only for China and the US, but especially for the European Union. The first thing to note is that although protectionism can never be growth enhancing, and certainly not for a net exporter like the EU, there are still gains to be made by European companies from the ongoing US-China trade confrontation in so far as they may be able to substitute US exporters into China or, less so based on our findings in this article, Chinese exporters into the US. Unfortunately, the current truce agreed between the US and Chinese governments at the sidelines of the G-20 meeting might reduce such opportunities for EU exporters and might even create trade diversion, again from European products and in favour of American products.

The fact that the EU feels increasingly squeezed between the US and China in their strategic competition should push us to ponder our options in the current global set-up. So far the EU's option seems to have been to support multilateralism at any cost. Unfortunately, the latter is increasingly less likely as the US has no intention to revert to the model which it once helped create. On that basis, and given Europe's reluctance to play a leading role without the US, the push for a return to multilateralism seems more an option of the past than an option of the future, let alone the present. The second most obvious option for the EU would be to increase its dependence on the US or, in other words, to push its strategic alliance further. However, we should realise that this comes at a cost, more specifically two concerns which were not present before. The first is the increasing unreliability of the US as an ally and its insistence on a seemingly different distribution of costs and benefits with its allies (more costs for the EU, such as military expenses, but fewer benefits on the trade side). The second caveat concerning a further reliance on the US is the need to align against China on issues of interest to the US. Although such issues are not too different from the complaints raised by the EU with respect to China (market access, reciprocity, excessive role of the state in the economy and a stronger defence of intellectual property rights), the reality is that the US interest will come first in this battle. In other words, the EU could lose its potential preferential access to China because of a stronger alliance with the US. Finally, the third option, namely rebalancing toward China, at least partially, cannot be an option for Europe in the current circumstances because of very limited access to the Chinese market. However, if China were really to further open up its economy to foreign competition (i.e., offer full market access), this option could become much more favourable. Based on past experiences since China entered the WTO, this option seems highly unlikely but worth pursuing. In that context, China's willingness to open up its markets to foreign competition clearly requires market access and reciprocity. While China makes up its mind on whether the above is a real option, the EU has no choice but to protect its strategic sectors from China's acquisitions and to safeguard the single market from unfair competition from Chinese SOEs.

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