

An EU-China trade war?

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The European Union has imposed punitive tariffs on Chinese electric vehicles, citing unfair subsidies as the reason. It may set off a wider trade war.



Picture credit: Financial Times

Introduction

It came as a surprise to many when, on 12 June, the [European Commission imposed punitive tariffs](#) of 38.1% on the import of Chinese-made electric vehicles (EV). “When our partners breach the rules, we will assert our rights,” stated EU trade Commissioner Valdis Dombrovskis. It was perhaps not so much the tariffs themselves that were surprising, but that they were so high. The Chinese EVs have been under investigation for a while, and the Commission has concluded that the level of subsidies breaks the principles of fair competition. The [tariffs will apply](#) not only to Chinese companies but also to those, like

Tesla, that produce their cars in China for export to Europe. Unless last-minute negotiations can create a mutually satisfactory solution, the tariffs will come into effect on 4 July.

Talk and writings abound about the ever-tense trade relations between the [United States](#) and [China](#). The Americans turned sharply away from free trade since 2016, while the Chinese have long faced accusations of duplicitous practices. The EU has long been the last defender of the open world economy, reluctant to limit trade and twice as reluctant to use large-scale subsidies. Just as it has successfully removed state aid from the European single market, it has sought to do the same globally. The change of tone is therefore all the more remarkable.

Long time coming

There has long been talk of unfair competition from China, where the state plays a very active role in the economy. The EU has had a constant trade deficit with China for many years. However, it really took off since 2020. In 2023, the deficit was a [staggering €291 billion](#), only surpassed by €397 billion in 2022. Not long ago, when most still considered globalisation a benign and beneficial process, this would not have caused concern. Today's climate is rather different.

The COVID pandemic exposed the vulnerability of complex supply chains, and we learned new words like '[friendshoring](#)' of critical industrial capabilities. As for China, and especially the EV sector and other green technologies, suspicions have long abounded of unfair subsidies and price dumping. [Experts estimate](#) the BYD company alone, today the world's largest EV producer, to have received more \$25 billion over three years. It has been the subject of several Commission investigations too. Few forget that subsidised competition from the US and China effectively put European solar panel manufacturers out of business. Today, [Europe imports 95% of its solar panels](#), most from China. Other than [investigations into Chinese practices](#) when bidding for contracts, the Commission looks intent on [holding the line](#) on no subsidies for the beleaguered domestic solar panel industry. There has also been mounting concern and Commission investigations over Chinese encroachment on the European pharmaceutical industry and its [procurement practices](#) for medical equipment.

What comes next?

Not surprisingly, Europeans are not entirely unified. France has been a proponent, while Germany has been the most opposed, its automobile industry being the [most dependent](#) on the Chinese market. German chancellor Olaf Scholz, long one of Europe's 'China doves', has launched into a last-minute [flurry of diplomacy](#) to help work the problems out. However, by all accounts, the Commission has solid backing from most EU capitals for a harder line.

The constant EU probes have angered China, which has signalled that food imports—cheese and wine, and especially French cognac—and aircraft may become [targets for retaliatory measures](#). Others fear that [China may hit back](#) by restricting access to rare earth minerals, something they already tried once last year when the US restricted exports of microchips. Some fear that countless small restrictions like this may be what [destroys trade altogether](#).

Interestingly, though, others argue that the tariffs are [nowhere near high enough](#) to counteract the level of subsidies China gives. The effect may merely be a slowing of Chinese imports. For the [full effect](#), tariffs would have to be in the order of 50%. Lastly, the whole question may become moot in time, as BYD anyway has plans, as part of its long-term strategy, to [establish production plants](#) in Europe, thereby effectively making the cars European.

Conclusion

The American experience from its near-trade wars with China in recent years is that [they are not](#), as Donald Trump famously put it, [“good and easy to win”](#). That is not to say that they must never be fought. After all, a higher price for actual security may be worth paying. However, one should not underestimate that a breakdown in trade relations between two of the world's biggest economies will be very messy and costly indeed. If, on the other hand, a longer-term consequence is that Chinese companies establish production in Europe, it will address a major European grievance.

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