

Short assessment of the federal government's China strategy

For a prudent alignment in relations with China



Berlin, September 2023

The federal cabinet approved a China strategy for the first time in mid-July 2023. In it, the federal government reiterates the three-dimensional assessment of China as a “partner, competitor and systemic rival”. The German Association of the Automotive Industry welcomes the fact that the China strategy takes into account both strategic and security interests as well as economic opportunities. For the German automotive industry, China is not only an important sales market and innovation location, but also an increasingly important supply market.

At the same time, the strategy paper shows a significantly changed perception of China in Germany. The end of the Corona restrictions now offers the opportunity to establish new trust and to address differences that have grown in recent years in direct dialogue. This explicitly also applies to critical issues such as compliance with human rights or the Taiwan issue.

Following the decision on the China strategy, the next step is to implement it. Accompanying this, the VDA has formulated the following recommendations:

1. Dialogue instead of isolation: Ongoing cooperation with China as a basic prerequisite for the successful implementation of the China strategy.
2. De-risking with a sense of proportion: As autonomous as necessary and as open, global and market-oriented as possible.
3. Bolster up Germany as an industrial location: Internationally competitive location conditions are the best insurance against growing competition and will strengthen resilience.

In the China strategy, the federal government announced that it would closely involve the Bundestag in the evaluation of the strategy paper – given the importance of German-Chinese relations, we believe this to be absolutely necessary. In addition, the China strategy envisages establishing a continuous exchange with business associations, companies, and unions to implement the strategy. With this position paper we want to support this idea and, analogous to setting up the “China Circle” of national State Secretaries, suggest an institutionalized exchange format with the participation of relevant stakeholders.

1. Dialogue instead of isolation

We welcome the fact that the federal government expressly commits to cooperation with China in its strategy paper. Cooperation is essential worldwide in view of the enormous challenges such as climate change and increasing technological fragmentation.

Intensify climate policy coordination: The establishment of a climate and transformation dialogue is a milestone in bilateral cooperation and an expression of the common goal of decarbonizing industrial processes, accelerating the energy transition and enabling climate-friendly mobility. The establishment must now be quickly followed by concrete implementation steps.

The climate cooperation between Germany and China has an important signaling effect for the international community. We strongly advocate that both sides intensify cooperation and set a positive example. China joining the climate club initiated by the G7 in Elmau would be such a signal. The federal government must also coordinate its climate cooperation with China closely regarding the high-level environmental and climate dialogue between the EU and China.

Continue cooperation in the area of electric and hydrogen mobility: China is increasingly developing into an innovation location for climate-friendly mobility – the fight against climate change ultimately benefits from this dynamic. As technology leaders, but also as major greenhouse gas emitters, Germany and China have a duty to lead the way here. Taking this into consideration, we support that the federal government and the Chinese government intend to continue cooperation in the area of electric and hydrogen mobility.

Automated and connected driving – counteracting technological fragmentation: Companies within the German automotive industry are performing pioneering work in the area of autonomous driving – this is also possible thanks to the innovative strength of Chinese partners and excellent local conditions. The know-how of Chinese researchers is also highlighted in the China strategy – the country is already a real lab for autonomous driving. The local commitment of the German automotive industry not only ensures its own competitiveness, but ultimately serves as a guarantee that technological advances are accessible worldwide.

We expressly welcome the fact that the federal government has clearly spoken out against decoupling in the technology sector in its China strategy. In this context, we are calling for the federal government to continue equal cooperation with the Chinese side regarding automated and connected driving.

Ensure security of business data streams: In its China strategy, the federal government honors the importance of free and trustworthy data flow between the two countries. Nevertheless, there is no mention of the Chinese cybersecurity law or the recent amendment to the anti-espionage law in China. Here, too, we rely on dialogue instead of isolation: We see the federal government as having a duty to advocate for the confidentiality of business, to address the extraterritorial effects of the laws and to find a solution together with the Chinese side.

Ensure cooperation also in standardization and norms: The close cooperation between Germany and China in setting standards and norms is an important pillar of bilateral relations. We are committed to ensuring that standards and norms are developed via the International Organization for Standardization (ISO) and the International Electrotechnical Commission (IEC) in an open, multilateral process. All partners are called upon to implement these standards unchanged in the national context. We call on the federal government to counteract nationalization tendencies in standardization and to support multilateral decision-making.

Dialogue requires personal exchange: Even after COVID19-related restrictions have been lifted, we are concerned that personal exchange between the two countries and the use of skilled workers are only hesitantly starting up again. We advocate that the federal government quickly creates additional staff capacity at the visa offices in China in order to cope with the volume of applications.

2. De-risking with a sense of proportion

The bilateral economic relations are a success story that have created prosperity, added value and employment in both Germany and China. It is therefore positive that the federal government is clearly rejecting “de-coupling”. However, it is also undisputed that the geopolitical environment has changed – the federal government is responding to this change with the concept of “de-risking”. However, such a risk reduction must not encourage the increasing construction of economic blocks – Germany, as a globally active export country, is dependent on open markets worldwide.

Maintain entrepreneurial freedom when making investment decisions: The members of the VDA examine possible business risks very carefully given the interdependence with China and strive for a high level of diversification and resilience. Companies’ diversification efforts can be supported and supplemented by government measures, but not directed. In this sense, we are open to confidential exchanges about risk analyses. However, we are critical of any further steps that may conflict with corporate sovereignty.

There are also open questions regarding the outbound investment screening planned by the European Commission – particularly regarding the positioning of the federal government. Here too, we are committed to respecting entrepreneurial freedom and would like to have a close exchange with the relevant institutions in this regard. Only in exceptional cases, when serious safety concerns are actually proven, government control intervention could be a last resort.

Balancing economic openness and public safety: Our industrial location is highly dependent on investments from third countries. An amendment to the investment review law must therefore ensure both: the protection of critical infrastructure and opportunities for foreign investors. It is important that such a reform – due to potentially lengthy review procedures – does not have a negative impact on the attractiveness of Germany as an investment location and is not specifically directed against companies from individual countries. Furthermore, Germany should not send any signal of increasing investment protectionism.

Strengthen the EU's strategic sovereignty in raw materials: The availability of raw materials is of particular relevance for the transformation of industry in Germany and Europe. However, a uniform, EU-wide monitoring of the supply situation must not reveal the vulnerabilities of raw material supplies in this country. The diversification of raw material supply chains can only be successful if new options are developed – this requires close exchange, particularly with countries in Africa, South America and the Pacific region. Additional raw material partnerships make it easier to develop new sources of supply and strengthen the strategic sovereignty of both Germany and partner countries rich in raw materials. In this sense, the federal government should take a strategic approach to expand further processing capacities within the EU and third countries rich in raw materials, e.g. by creating a European raw materials agency and a raw materials fund.

De-risking needs more free trade: In order to best support companies' diversification efforts, we need free and fair trade. It is therefore up to the European Commission to conclude and implement new trade agreements promptly. Negotiations with Mercosur, Mexico, ASEAN and India should be concluded as quickly as possible. To this end, trade agreements must not be overloaded with other topics, otherwise the partners' willingness to conclude a deal with the EU will decrease. The federal government must appear with one voice in Brussels and support the plan to open up new markets through targeted political support and high-level delegation trips.

3. Bolster up Germany as an industrial location

The German automotive industry – manufacturers and suppliers – is a driving force for research and development worldwide. Accordingly, we look confidently at the growing global competition – also from the Chinese side. Despite this, concerns about the competitiveness of Germany as an industrial location are increasing. The debate on China is important, but it should not obscure the tasks here on side. In order to strengthen the competitive position and to secure new investments, the federal government must improve the framework conditions for Germany as a location.

Accelerate energy transition: Companies need competitive energy prices, security of supply, accelerated expansion of renewable energies and additional international energy partnerships. This is a prerequisite for the ramp-up of electromobility and the associated charging infrastructure.

Create a competitive tax and duty system: The state burden on energy use, especially electricity, must be quickly reduced to an internationally competitive level. Non-wage labor costs are also increasingly becoming a hurdle for many companies and are putting a strain on liquidity, especially in medium-sized companies. In addition, corporate tax law urgently needs to be freed from excessive bureaucratic requirements and digitalization needs to be promoted.

Alleviate lack of skilled workers and labor shortages: The lack of adequately skilled workers and laborers is massively affecting the growth opportunities of many member companies – in particular, small and medium-sized companies in the automotive supplier industry are desperately looking for staff. In order to remain globally competitive, also in the face of the demographic development, we need a qualification initiative to prepare skilled workers for the requirements of future technologies.

Reduce red tape, promote digitalization: Administrative processes are too lengthy, complex and not digital enough – this deters German as well as foreign investors. In addition, new and stricter reporting requirements – such as potentially the EU Corporate Sustainability Due Diligence Directive – are putting pressure on companies. The federal government should assert its influence in Brussels and implement the announced national moratorium on burdens.

Contact persons

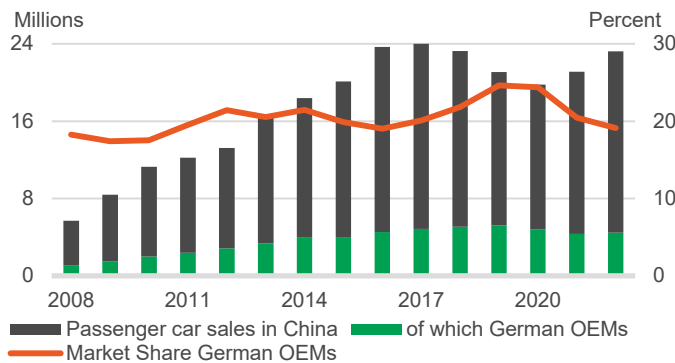
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On the automotive industry in China

1. The importance of the market

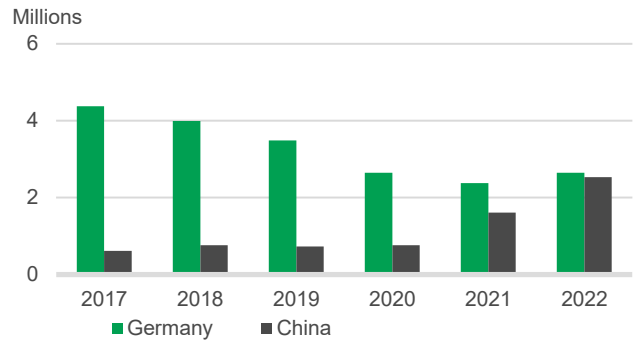
Passenger car sales in China



- Today, **almost one in five new cars** in China bears the logo of a German corporate brand. In absolute numbers that means: in 2022, German manufacturers sold **around 4.4mn cars** in China.
- The German automotive industry **was able to benefit** proportionally from the major growth over the past decade.

2. Car exports in comparison

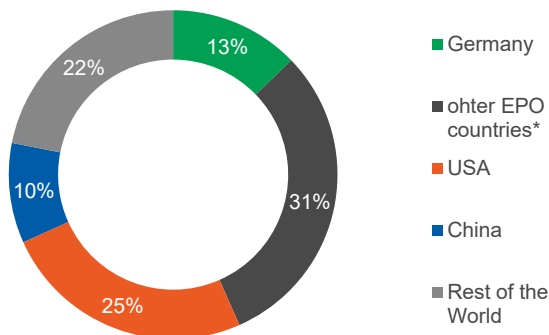
Passenger Car exports from Germany and China



- After Japan, Germany is the largest car exporter in the world. Most recently, in 2022, 2.6mn cars manufactured in Germany were then exported abroad. This means that **three out of four cars from German factories go abroad (76%)**.
- **China has been able to significantly expand its car exports** in recent years - but is still behind Germany with 2.5mn cars exported. **The export quota for passenger cars made in China is 11%.**

3. Research & Development

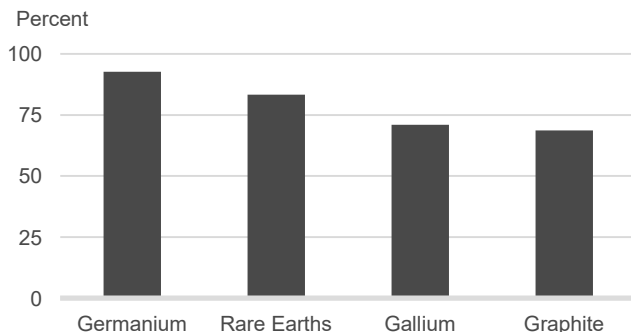
Origin of patents registered in Europe



- In 2022, the European Patent Office (EPO) registered 193,500 patent applications. Of these, **13% came from Germany** and 31% from other EPO countries. **10% came from China**. China has therefore become an important technology partner.
- **German companies play the leading role in the transport sector (20%** of all patent applications in the transport sector). **Chinese companies filed 7% of all transportation patents.**
- **China is particularly strong in the area of digital communications technologies (28% share of sector-specific patent applications).**
- Many German companies conduct research for the Chinese market in Germany.

4. Raw materials

China share in the import of selected raw materials



- **More than 90% of Germanium**, which is highly relevant in the production of electronic components, is imported from China.
- **More than 80% of rare earths** - which are particularly important for the ramp-up of electromobility - **come from China.**
- For the question of dependency it is also relevant to what extent the supply could be replaced in short term through imports from other countries or domestic production.
- **For many important raw materials needed for electromobility ramp-up, China occupies a central position in the supply chain.**

China is the largest single passenger car market in the world. The German manufacturers and suppliers have been involved in China for a long time and were able to secure a good market position. The VDA is also present in China and has had an office in Beijing for nine years. China is increasingly emerging as a competitor on international markets. The research power of Chinese companies is also growing. Especially for raw materials important to the ramp-up of electromobility, China plays a central role in the supply chain.

The German Association of the Automotive Industry (VDA) consolidates more than 650 manufacturers and suppliers under one roof. The members develop and produce cars and trucks, software, trailers, superstructures, buses, parts and accessories as well as new mobility offers.

We represent the interests of the automotive industry and stand for modern, future-oriented multimodal mobility on the way to climate neutrality. The VDA represents the interests of its members in politics, the media, and social groups. We work for electric mobility, climate-neutral drives, the implementation of climate targets, securing raw materials, digitization and networking as well as German engineering.

We are committed to a competitive business and innovation location. Our industry ensures prosperity in Germany: More than 780,000 people are directly employed in the German automotive industry. The VDA is the organizer of the largest international mobility platform IAA MOBILITY and of IAA TRANSPORTATION, the world's most important platform for the future of the commercial vehicle industry.

If you notice any errors, omissions or ambiguities in these recommendations, please contact VDA without delay so that these errors can be rectified.

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