



GERMANY IN THE WORLD: CHALLENGES & OPPORTUNITIES



Meeting the China Challenge with Bolder Action

Germany Should Diversify Its Economy and Protect Its Technology

By Didi Kirsten Tatlow

The German government has vigorously driven its relationship with the People's Republic of China (PRC) forward over the last few decades. In 2017, China became Germany's single largest trading partner, not counting the EU. Yet, in 2019, Europe identified China as a "[systemic rival](#)," based on the Great Power ambitions of its rising dictatorship to leverage trade for political gain, conduct aggressive [cyber espionage](#), steal technology, massively breach universal human rights standards, and change the international order. Because of Germany's economic relationship with the PRC, German industry and government believe it is nearly impossible to oppose such behaviors openly that – taken together – threaten Germany's long-term prosperity and democratic security. Diversifying from China to include wider political and security considerations in policy will not be easy, but it is necessary and overdue.

The rise of the People's Republic of China (PRC) since 1978 to become the world's second biggest economy happened with the broad political, technological, and societal support of Germany and other industrialized nations. For decades, German economic and foreign policy toward China was driven by the principle of *Wandel durch Handel* ("Change through Trade"). High-profile German corporations – particularly in the auto, chemical, and engineering sectors – as well as the smaller companies of its *Mittelstand* invested enthusiastically in the PRC. In 2020, bilateral trade between Germany and the PRC stood at €212 billion.

Despite the obvious economic rewards, the risks of dependency on a non-democratic nation that does not respect the rule of law are real and

long-term. For example, China openly leverages trade for political gain. The PRC is currently applying trade bans on Lithuania for upgrading its relations with Taiwan, which China threatens to invade, while Chinese state media issues [political threats](#) – the first time it has taken such open action in Europe. China also punished Australia with about a dozen official and unofficial trade bans and massive cyberattacks on Australian institutions when it pushed back against Beijing's political interference and called for an independent investigation into the origins of the virus that causes COVID-19. However, Australia has already been able to [recoup](#) 80 percent of the foreign trade lost to these bans. Another indication that Australia is at the forefront of political and trade tensions with China is the recent creation of AUKUS, a trilat-

eral security pact among Australia, the United Kingdom, and United States; it highlights how a failure to change direction in Germany could increasingly sideline it among world democracies.

Under the leadership of the Communist Party of China (CPC), the country is neither a free trader nor will it become one. Rather, it is growing dominance strategies in multiple areas. In October 2020, President Xi Jinping said that China aimed to deepen the world's dependencies on its industrial supply chains; in March 2021, Premier Li Keqiang voiced the ambition to turn China into a "powerful gravitational field" that cannot be resisted. Talk of "decoupling" is misplaced; in reality, China never "coupled," posing a range of political and economic challenges for the world. Today, it is again turning inward.

Behind closed doors, some senior German business figures have started asking if Germany is held hostage by China's market. Recognizing the need to diversify, the German government published its [Policy Guidelines for the Indo-Pacific](#) in 2020 to nudge Germany away from its decades-old focus on China in Asia toward other relationships and economic ties in the western Pacific and Indo-Pacific. In addition to Australia, Japan and even South Korea have begun quietly re-orienting away. Such a realignment by Germany would strengthen the transatlantic alliance and, by extension,

dependencies [worsening](#). Closer scrutiny and better risk management are needed – so are targeted technology controls, since Germany has long failed to protect its technology and knowledge outflow to China.

In 2015, Beijing published its “Made in China 2025” plan to [replace](#) Germany as the go-to manufacturer of quality goods. Specifically, the plan aims for China to dominate in ten key industries, including e-cars, IT, aerospace, machine building of different kinds, and medical technology. The PRC also has a state-driven plan for

this is not nothing, Germany must look more to its long-term prosperity – especially given China's new economic strategy of “[dual circulation](#),” a form of import substitution and further decoupling that is increasing pressure on German companies to localize in China, hand over more intellectual property, and transfer research and development. Under China's system of “[military-civil fusion](#),” it is unfortunately impossible to firewall cooperation in science and technology from military use.

Protecting human rights will also drive diversification. Today, key German companies, including BASF and Volkswagen, operate factories in China's Uighur regions – this is demanded by Beijing as a price for having factories elsewhere in China and is another example of how the CPC purposefully manipulates economic ties. Chinese officials have said that the PRC aims to “break the roots” of its Uighur peoples, who are subjected to human rights violations that include forced labor. The activities of German companies in China have begun to be legally challenged at home by civil society actors and will face more challenges via Germany's *Lieferkettengesetz*, its [supply chain law](#). The latter carries penalties for German companies involved in slave labor. Therefore, German companies in China need to create greater congruence between their financial interests abroad and their ethical and political values at home to avoid being penalized. The German Bundestag can play a key role in creating democratic pressures on Chinese government and industry to adhere to crucial human rights standards.

China Has Overtaken Germany in Its Share of World Exports

World Export Shares of Goods and Services in Percent

	2000	2019
China	3.20 %	10.80 %
USA	14.10 %	10.20 %
Germany	7.70 %	7.40 %
France	5.00 %	3.50 %

Source: OECD 2019; German Economic Institute

NATO. Its timing would be fortuitous, as some observers believe that Xi is preparing his country for war with Taiwan. Indeed, driven by China, the political, economic, and military risks in Asia and the Indo-Pacific are growing.

DETERMINING FACTORS German Economics and Chinese Politics

According to one study, Germany has built up [dependencies](#) on China in approximately 100 categories of goods since 1978. As China begins to overtake Germany in the manufacture of exports, it is in Germany's interest to diversify and explore new markets and production sites to avoid

industrial-strength artificial intelligence, the “China Brain Project 2030.” In addition, it is working on “China Standards 2035,” which will offer an alternative to Germany's global industry standards yet is being created with German support.

German diversification away from its growing dependence on China will not and cannot be quick, but it must begin immediately. It requires political leadership and should focus on allies. Overall, it is important to remember that only 8 percent of German exports go to China while 67 percent go to Europe. Volkswagen sells 40 percent of its cars in China but may make [only 20 percent](#) of its profits there. Although

CHALLENGES Managing China Politically and Economically

Germany needs to acknowledge that it – along with the rest of the world – is in uncharted waters with China.

The “Made in China 2025” Policy Aims to Dominate in 10 Key Sectors China Would Replace Germany as the Go-To Manufacturer of Quality Goods



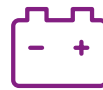
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OCEAN
ENGINEERING



NEW PHYSICAL
MATERIALS



RAILWAYS



BIOTECHNOLOGY
AND MEDICAL
EQUIPMENT

Source: State Council document no. 28, “Made in China 2025,” published May 19, 2015

After the new German government is established, it should move fast to set up a national security review of the direction China is going and what that means for Germany, politically and economically.

The new Bundestag can work to support safer investment destinations, pushing for a bilateral investment treaty with Asian countries including Taiwan. Crucially, it should put policies into place that enable promising German companies, especially those in high-tech and specialized economies, to invest more in the future of Germany and its neighbors. It should also follow the example of the European Parliament and push to upgrade relations with Taiwan to raise the price of invasion for Beijing.

Perhaps most importantly of all, Germany needs to stop its virtually untrammelled flow of technology to China, which is not only deeply harmful to German competitiveness but also to the investment Germany and the European Union are making in educating people. For decades, China has made the handover of the technology used to manufacture goods a condition for German companies to manufacture – a practice known as forced technology transfer. Despite the fact that this practice was barred when China joined the WTO 20 years ago and, again, in the Comprehensive Agreement on Investment (CAI) between the EU and China agreed in December 2020, the ban will continue to fail. China is building up its own skills, but it is still too depen-

dent on foreign technology for economic growth, too intent on procuring what it needs, and too determined to avoid fully integrating with the world to abandon the practice. Also, technology transfer “by multiple ways and means,” as Chinese ministries officially describe it, has virtually no costs because the sources of technology, such as Germany, do not impose such costs or resist. Consequently, Germany urgently needs to take steps to push back against a total of 32 methods employed by the Chinese party-state to gather and transfer technology to China. Stopping the loss of technology and certain types of high-tech or specialist talent from its research institutions, universities, and companies would preserve Germany’s own democratic and economic – that is,

systemic – advantages. The next federal government and its legislature should do the important work of looking much more closely at legal, illegal, and gray-zone technology transfer and strengthen existing regulations to control it, including through law enforcement agencies.

RECOMMENDATIONS

A Multi-Pronged Approach

The new German government and Bundestag should support efforts to:

Diversify away from China by examining Germany's foreign trade and tax policies, thus creating preferential conditions for investment outside of China. Because Taiwan is a source of important manufacturing components, such as semiconductors, it is in Germany's interests to strengthen this relationship and support efforts by the European Parliament to upgrade relations with Taiwan.

Highlight core human rights issues and pay greater attention to intimidation tactics, such as surveillance and threats to both Chinese persons and non-Chinese citizens in Germany. In this way, the rights of Chinese citizens, including Uighurs and Hong Kongers, are better protected globally – in contrast to the pressures and risks they face in China. Focusing on core values will naturally lead to closer alignment with allies. The new German government should also rapidly expose apparent efforts by China to bribe Bundestag members or otherwise interfere in hidden ways in German society.

Question inbound investments from China even more carefully by seeking scrutiny and advice from experts and research institutions. Germany should move quickly to improve its own inward investment screening mechanism, which is not sufficiently conscious of national security. Two recent developments illustrate why: first, an investment by China Logistics,

a centrally state-owned firm, in the Jade-Weser-Port at Wilhelmshaven, which is in close proximity to the German Navy's own major port and logistics hub; and, second, a possible investment by the state-owned Chinese shipping company COSCO in the Port of Hamburg. Such investments are not reciprocated by China; it is time to end them in Germany. China frequently emphasizes the concept of "mutual respect" – this should translate into reciprocity.

Invest much more in itself, its neighbors, and allies. Germany must become much better at commercializing the technologies it develops instead of allowing them to be transferred elsewhere, thereby losing control of both the technologies themselves and market share. It makes no sense that talented German startups feel they must turn to China for venture capital because they cannot get support in Germany.

Scrutinize students from the PRC and their research activities more carefully. Germany should continue to welcome students and researchers from China in the humanities and social sciences, including such fields as sociology, law, politics, literature, and the arts. However, the new government should consider barring them from key research areas such as robotics, cybernetics, aerospace, or oceanic research – all of which have a high relevance for China's military-civil fusion system.

In this memo series, DGAP offers concise analysis of issues related to foreign and security policy that will shape the agenda of Germany's next legislative period. Each memo provides insight on how the new federal government and parliament can take advantage of opportunities and meet challenges as European and global dynamics grow increasingly complex. Topics include technology, climate, migration, the international order, security, and geo-economics.

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