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De-risking from China and Its Implications

By Amrita Jash

SYNOPSIS

De-risking has become the new buzzword. Amidst rising tensions with China, the major western powers are opting to de-risk and not de-couple in dealing with China. This makes it imperative to understand: What does it mean to de-risk from China and what are the likely implications of it?

COMMENTARY

On 13 July 2023, the German government published its first-ever document titled "[Strategy on China](#)". Embedded in the aims and principles of the European Union's (EU) common policy on China, the strategy claims to be a "means of enhancing a coherent European policy on China".

Exemplifying a shift in Germany's perception of China, the document reads: "China has changed. As a result of this and China's political decisions, we need to change our approach to China". While the document specifies that Germany is not seeking to engage in "any decoupling" with China, it strongly posits that "[de-risking is necessary](#)".

Referring to China as a "partner, competitor, and systemic rival", the document explicitly states that while Germany accepts "competition" with China, there are serious "concerns" over how China is attempting to influence the international order in line with the interests of the Chinese Communist Party, as exemplified by China's decision to further its relations with Russia and its increasing assertiveness in the Indo-Pacific for regional hegemony.

This German strategy is in alignment with the "de-risking" calls by the US, the G7 countries and the EU.

De-risking but not De-coupling

The term “de-risking from China” was first put forward by [President of the European Commission \(EC\)](#), Ursula von der Leyen, in a speech on EU-China relations on 30 March, where she said: “Our [EU-China] relations are not black or white – and our response cannot be either. This is why we need to focus on de-risk – not de-couple”.

After that, the US government, the G7 and the EU have mentioned or referred to the de-risk strategy, as for instance, in May 2023, when the [G7 Hiroshima Leaders' Communique](#) publicly endorsed the objective of “de-risking and diversifying” away from China to maintain “economic resilience” but “not decoupling or turning inwards”. Similarly, on 30 June, the [EC](#) stated that the EU “will de-risk and diversify where necessary and appropriate” but “does not intend to decouple or to turn inwards”.

Why De-risk?

The EU's concerns about overdependence on China can be discerned from the following trends.

China is one of the [EU's top trading and investment partners](#). It is the third largest destination for EU exports, and the largest partner for the EU in terms of imports (20.8 per cent). Especially with Germany, China is the fourth-largest recipient of German exports (7 per cent) and is Germany's most important source of imports (12 per cent).

Furthermore, [two key aspects loom large](#): First, the EU imports 90 per cent of its lithium – besides other rare earths and critical minerals that are crucial for battery technology and green energy transition – from China. Second, is the vulnerability attached to the dependency on Taiwan, which provides more than 90 per cent of the EU's need for advanced semi-conductors, and which poses a concern in the event of a cross-Strait crisis.

The German document also cited the need for Germany to reduce its dependency on China in critical areas such as medical technology, medicinal products, rare earths, preliminary products needed for energy transition, amongst others, given the vulnerability of the supply chains that surfaced during the COVID-19 pandemic and tensions in the Taiwan Straits.

To de-risk, the EC in March 2023, proposed the [Critical Raw Materials Act](#) to “end dependencies on just one or a few countries” and to “ensure the highest level of diversification of supply chains for our European businesses”.

China's Reaction

In Beijing's view, however, the “de-risking” rhetoric is based “on a false narrative”. Chinese Premier Li Qiang criticised it as the [West's idea of “forced proposition”](#). And, in response to Germany's China Strategy, [Chinese Foreign Ministry Spokesperson Wang Wenbin](#) stated, “To shut out China in the name of ‘de-risking’ is to throw away opportunities, stability and development. Such a move would only create and spread risks, and no one would benefit from it”.

This statement resonates with former foreign minister [Qin Gang's words](#) at a joint press conference with German foreign minister Annalena Baerbock, where he posited: "If the EU seeks to decouple from China in the name of 'de-risking', it will decouple from opportunities, cooperation, stability, and development".

The [Chinese Embassy in Germany](#) also issued a statement, saying: "Forcibly 'de-risking' based on ideological prejudice and competition anxiety will only be counterproductive and artificially intensify risks".

Implications of De-risking

While building new supply chains is the need of the hour, it is also costly and time consuming. Where Germany and its allies are concerned, there is no other option.

Given the growing risks and volatile operating environment caused by the pandemic, Russia-Ukraine War, concerns over Taiwan, the intensifying US-China rivalry, etc., the immediate implication of de-risking is the shifting of investments out of China.

According to the "[Business Survey 2023](#)" of the European Union Chamber of Commerce in China, 11 per cent of respondents have shifted investments out of China; 8 per cent shifted investments previously planned for China to elsewhere; and 10 per cent have already relocated, or plan to relocate, their Asia headquarters away from China. It is also interesting to note that apart from European companies, almost four in ten (38 per cent) of Chinese customers and/or suppliers have also shifted investments out of China.

In this de-risking process, the ASEAN region has become the "destination of choice", i.e., the main beneficiary, of the investment shifts out of China. As per the survey, the top destination for companies moving their Asian headquarters out of China was Singapore, with 43 per cent of companies that moved, followed by Malaysia. Only 9 per cent went or plan to shift to Hong Kong.

Thus, what has been achieved is that China is no more the top destination for investments. This has come on top of the increasing difficulty of doing business in China brought about by the political environment, economic slow-down and stringent security controls.

Therefore, the West's de-risking from China provides opportunities for other countries in Asia to become nodal points in the re-configuration of the global supply and value chain.

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