EU ECONOMIC SECURITY:

CONFRONTING THE DUAL CHALLENGE OF CHINA AND THE US

Cinzia Alcidi,

CEPS, Senior Research Fellow

A deeply changing and uncertain landscape

Changing geopolitical environment

- Growing conflicts and the US retreat from global leadership
- Emerging new alliances?
- EU uncertain role

An uncertain global economic environment

- The new central role of geoeconomics:
  - Use of economic linkages to achieve geopolitical objectives, or geopolitical power to gain economic advantage
- What future for trade?

Quest for security in an insecure world

Large countries have sought to reduce external reliance for years

2015 “Dual circulation strategy” and ‘Made in China 2025’

America first, MAGA

2014 ‘Make in India’

Europe has remained faithful to openness and free markets (until now..)

But now economic security and the search for strategic autonomy have become key priorities

How does this complex context translate into challenges?

Theory vs. reality

Key pillars of current economic growth are falling. We have moved away from:

- Rule-based system: certainty and reciprocity
- Market-driven economy: efficiency

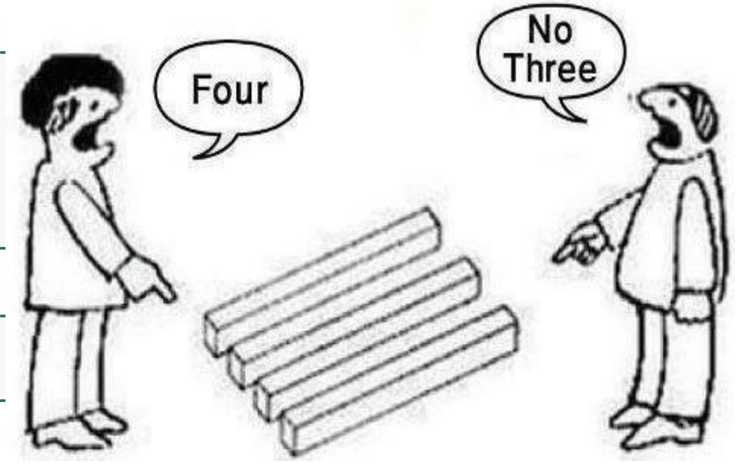
Economic theory: Expect negative impacts on the economy

- On the US economy, thought tariff-induced inflation, inefficiencies and reduced credibility
- On the EU and global economy through trade disruption (e.g. GVC) and financial linkages

Reality until now:

- US economy is doing quite well and the stock market performance is stunning
- Global economy and global trade are showing impressive resilience

Are politics trumping economics?



"In economics, things take longer to happen than you think they will, and then they happen faster than you thought they could" (R. Dornbush)

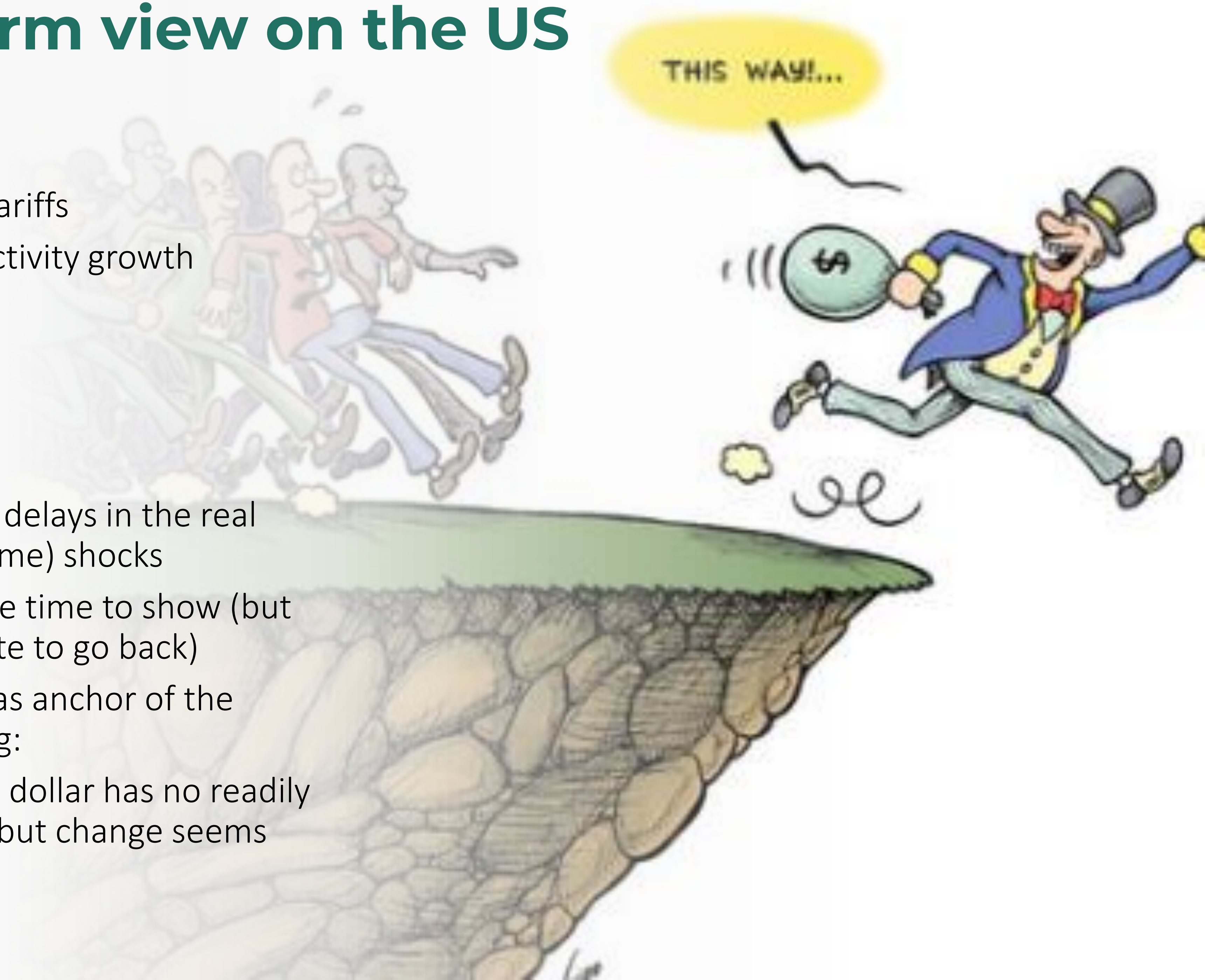
Short vs. long-term view on the US

Short-term optimistic view

- The global economy can stand tariffs
- AI will lead to impressive productivity growth
- No concern about US debt

Longer-term, less optimistic view

- Time lag:
  - Anticipatory behaviour and delays in the real economy reaction to (extreme) shocks
  - Institutional disruptions take time to show (but when they show, it is too late to go back)
- The US and the US dollar's role as anchor of the global financial system is shaking:
  - It's taking time because the dollar has no readily available alternative today, but change seems inevitable



A closer look at the US economy: beneath the glitter

No inflation – no problem,
but... some prices are rising

Markets are calm, but... it may not last

Consumers are still spending,
but...only at the top

The labour market is stable, but... signals point to weakness

A closer look at the US economy: structural risks

The tariffs damage

- Broke the international trade system
- Revenues unlikely to address US fiscal imbalances, but tariffs will stay
- US reindustrialisation is extremely unlikely despite claims and “forced“ foreign investments

The attack on the Fed

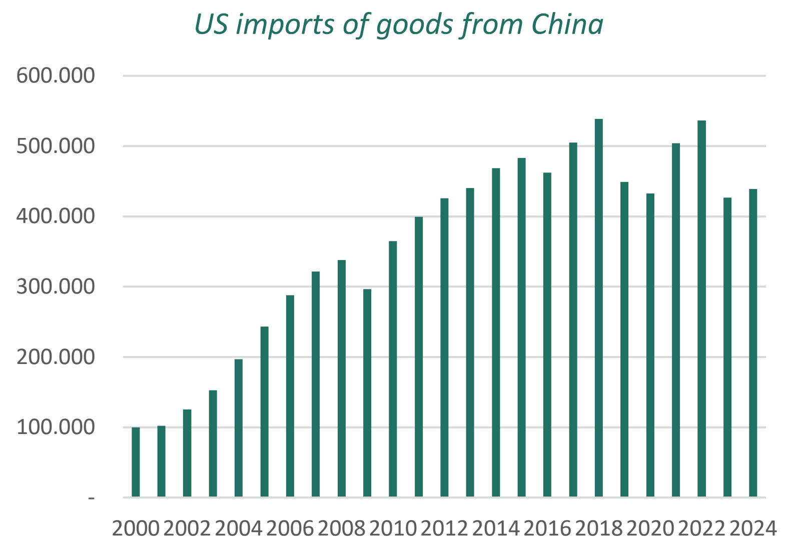
- Government to control the Fed and a plan to suppress independent government agencies
- Privatisation of money issuance – end of the singularity of money
- Increasing risk to the Fed’s and USD credibility as global anchors
- Financial stability risks– elimination of safety nets

Free markets no more

- Growing state intervention
- Politicisation of markets
- Abuse of the national security instrument
- National vs. private interests

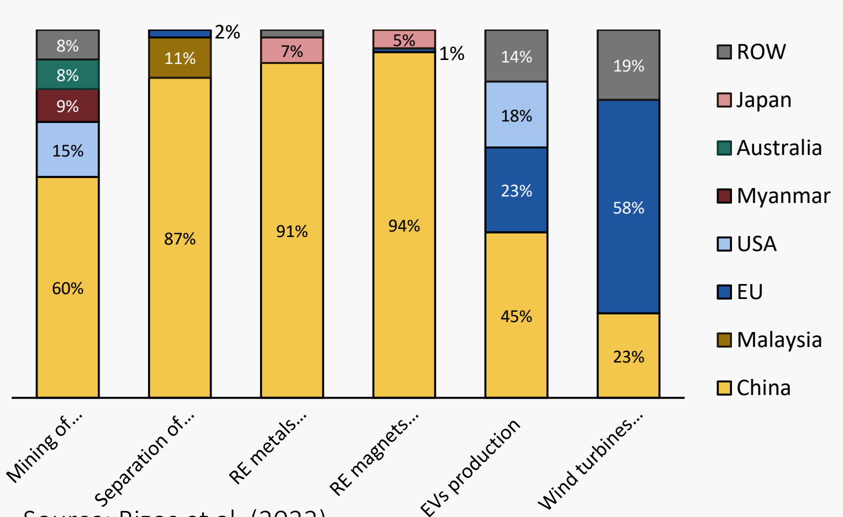
The US-China power competition

China refused to negotiate and retaliated



Source: FRED

Geographical concentration of the rare earths permanent magnets VC



Source: Rizos et al. (2022)

- Why is China the US's strategic rival?
  - Large deficit: $440 bn in US imports of Chinese goods (2024)
  - Geopolitical rivalry: Strategic competition for global influence.
  - US Domestic politics: Bipartisan scepticism toward China in the US Congress.

- China's strategic bet
  - Leverage over supply chains and dominance in raw materials.
  - Underestimation of US reliance on Chinese goods.
  - Reindustrialisation in the US faces significant structural challenges
  - Underestimation of China's growth potential

- What next?
  - Unambiguous signals: multiple trade truces, but persistent tensions

What does this mean for Europe?

EU internal politics and geopolitics

- The EU's multi-level governance and country heterogeneity are resulting in a lack of unity and slow decision-making.
  - This makes democracy look a second best compared to autocracies, where decisions are fast and centralised – this is a fundamental challenge for Europe and democracy
- Being a soft power in a world dominated by power politics means weakness
  - The EU needs to find a new paradigm to define its role in the global scene
  - Openness and being a standard setter are not enough anymore

Security and defence

- Security is the EU's Achilles' heel
  - Dependence on NATO and a less reliable US, combined with increasing threats from Russia, is not acceptable anymore
  - EU has been unable to make its own choices and leverage its economic strengths

EU trade redux (I)

US tariffs are there to stay ..

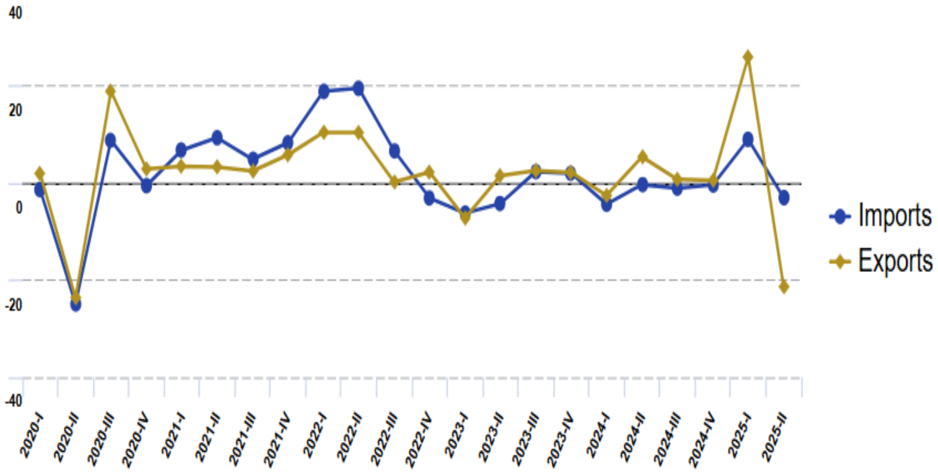
- Trade has not stopped; rather, flows have been reoriented
- The world (exc. China and Canada) has not responded to Trump's tariffs with tariffs
  - The US-China truce, but uncertainty is high and tensions have not fallen

---

- The impact of US tariffs on the EU exports is, for the time being, limited, but it is still too early to say
- The EU-US trade agreement is not yet finalised – Political deal = "gentlemen's agreement"
- EU committed to removing its tariff barriers – de facto very small (except on automotive), very limited impact
  - Does it apply only to the US or all trade partners?
- Open question: capacity to pass on the tariff without losing market access – depends on US consumers/businesses
- EU commitments to invest in the US are still uncertain – new vs. planned, government vs. private sector
- Commitments to the gas purchases are also uncertain

EU trade in goods vis-à-vis the US

Quarterly growth rates (%)



Source: Eurostat

EU trade redux (II)

EU-China trade relations are tense

- Economics:
  - China is a key EU trade partner – crucial for some EU industries and for the supply of raw materials
  - Chinese government's support for the domestic industry is problematic for the EU and its companies
  - EU concerns about oversupply impacts
  - Increasing EU industry pressure to protect domestic manufacturing - restoring a level playing field
  - Is the WTO still relevant?
- Beyond economics:
  - China-Russia "unlimited friendship" is a major issue for the EU

EU trade redux (III)

Is EU openness is deemed to decline?

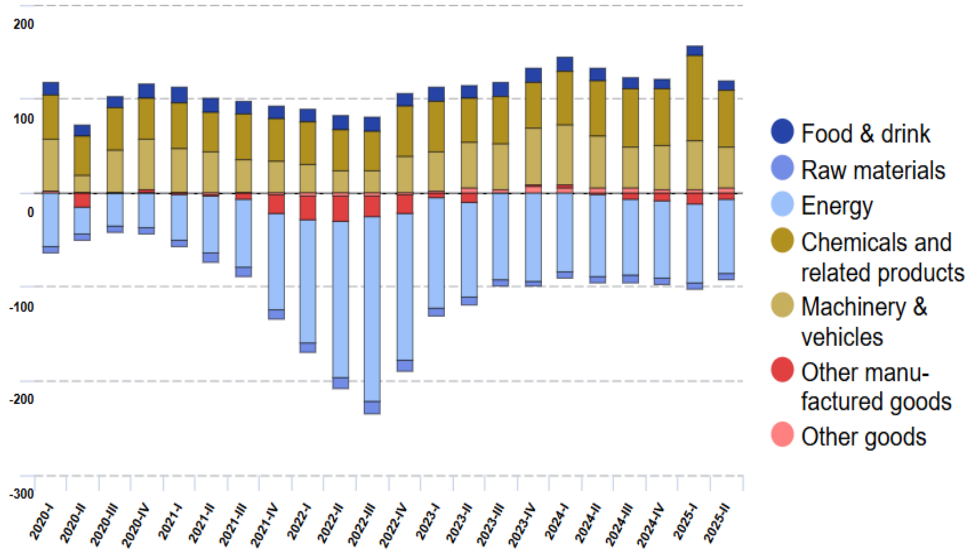
- Increasing bilateral agreements (e.g. Mercosur, EU-India)
  - Will they work? What about a WTO 2.0?

- EU energy dependency
  - remains an issue for competitive manufacturing

- EU domestic investment needs to increase, and this is incompatible with the large current account surplus of the last decade

Extra-EU trade balance in goods, by product group

Euro Billion, quarterly



Source: Eurostat

From US-led order to fragmented multipolarity

- Transition from a US-centred hegemonic order to a multipolar world marked by weak multilateralism and rising nationalism.
- Companies' decisions are no longer driven purely by economic efficiency or by assumptions of full mobility of people, goods, services, capital, and resources.
- Rival blocs are emerging— loosely defined and shifting in composition ("variable geometry").

Thank you!

www.ceps.eu

cinzia.alcidi@ceps.eu

@CEPS_thinktank

cinzia alcidi

EU economic security: confronting the dual challenge of China and the US

Risks and opportunities in evolving EU–US financial and economic relations