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Europe and China's economic reorientation

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At the last summit of the two sessions in March 2025, China again set an annual growth target of around 5%. Some analysts are questioning these figures[1] and even more so the sustainability of such a pace. In fact, the engines of Chinese growth are in crisis: the real estate sector has been in decline for four years now[2][3] and the level of exports, which have reached a record in 2024[4] , will be unsustainable in 2025 against a backdrop of a general increase in customs duties. The challenge for the authorities is therefore to succeed in offsetting the fall in exports by stimulating domestic consumption. Indeed, maintaining a high growth rate is a major challenge for Beijing, which priority is to preserve economic and social stability.

I • Stimulating domestic demand: the priority for 2025

At the Two Sessions Summit, the government's activity report highlighted domestic demand as the "main driver" (主引擎) of growth, in the words of the regime's number two, Li Qiang. To achieve this goal, the central government is planning a stimulus package of more than 1,300 billion yuan (€152 billion), via special very long-term bonds[5]. In addi-

1 The Rhodium Group estimates that China will grow by between 2.4% and 2.8% in 2024. See Daniel H. Rosen, Logan Wright, Jeremy Smith, Matthew Mingey and Rogan Quinn "After the Fall: China's Economy in 2025,

2 See this article in the Financial Times, which dates the start of the crisis to Evergrande's bankruptcy in 2021, https://ig.ft.com/china-property-crisis/

3 According to the IMF, the property sector will account for 13.7% of China's GDP in 2021. The crisis in this sector is leading to at least 2% less GDP growth per year, not to mention the problems of financing local government debt, https://www.imf.org/en/Publications/fandd/issues/2024/12/chinas-real-estate-challenge-kenneth-rogoff

4 See State Council announcement, January 2025, https://english.www.gov.cn/archive/statistics/202501/13/content_WS6784a546c6d0868f4e8eec59.html

5 In addition, China has earmarked 300 billion to specifically target consumption in certain sectors, https://www.reuters.com/world/china/chinas-parliament-meets-shield-economy-us-tariff-salvos-2025-03-04/

tion, the provinces are authorised to issue additional loans themselves.

However, a comparison with the 2008 recovery plan (480 billion euros, three quarters of which was financed by local authorities) shows just how much the situation has changed. By 2025, many provinces and municipalities will have no room for manoeuvre because of the real estate sector crisis and the increase in their debt. The final figure for investment will therefore probably be much lower than the Chinese government forecasts.

Another issue concerns the very nature of this spending. Rather than financing households directly, leaving them free to decide what to consume, the government is giving priority to subsidising the purchase of targeted material goods (household appliances, digital equipment). However, these sectors are already suffering from overcapacity: if demand is not there in earnest, there is a risk of further excess production, contrary to the stated aim of sustainably supporting domestic demand.

II • The birth rate, an indirect driver of consumption

To boost demand, Beijing is also counting on an increase in purchasing power and the birth rate. The government is promising a (modest) increase in the minimum retirement pension of 143 yuan a month (€18), a reassuring political message for households but of limited scope.

In a bid to halt the fall in the birth rate, Beijing is also banking on free pre-school education and family allowances. Some provinces, such as Inner Mongolia, now offer 10,000 yuan (€1,250) for the first child and up to 100,000 yuan (€12,500) for the third child. However, once again, these measures depend on the financial health of each province to fund these bonuses, amplifying the territorial disparities that already exist. Added to this are structural problems – precarious working conditions, recurrent cases of dismissal in the event of pregnancy – which simple financial incentives are not enough to resolve.

III • Local government debt: swaps as a way out?

The drive to boost consumption is also coming up against local government debt. Deprived of their main tax revenues following the collapse of the property market, many local authorities are even struggling to pay their civil servants and teachers. To avoid a widespread default, Beijing is promoting a "debt swap" mechanism: replacing expensive short-term loans with special longer-term bonds backed by the central government.

While this technique provides temporary relief for local budgets, some economists fear that it will postpone the problem and encourage the provinces to multiply their off-balance sheet commitments. Without far-reaching tax reform (e.g. through the introduction of a council tax) or a reduction in public spending, the problem may simply be put off until later, at the cost of ever higher overall debt.

IV • A welfare state still a long way off

For some experts Western[6], the creation of a genuine welfare state would be the most direct solution for stimulating Chinese consumption. Securing access to healthcare, education and pensions would encourage households to save less and spend more, thereby kick-starting the economic machine. Beijing remains reluctant to take this step, however, for a number of reasons.

On the one hand, since 1989 – the year of the Tiananmen Square crackdown – the legitimacy of the Chinese Communist Party has been based above all on economic performance. The survival of the regime takes precedence over the development of a social system. In this context, any economic policy likely to pave the way for a welfare state - and with it the rise of greater social expectations,

6 See the speech by Janet Yellen, former US Treasury Secretary, https://china.usembassy-china.org.cn/remarks-by-secretary-of-the-treasury-janet-l-yellen-at-a-press-conference-in-beijing-the-peoples-republic-of-china/

potentially difficult to channel - is seen as a risk factor. It should be remembered that the first wave of pro-demand policies coincided with a series of killings at the end of 2024, notably the one in Zhuhai[7], which may have helped to dampen political enthusiasm for these measures.

Beijing fears that the development of a universal social protection system could lead to the emergence of a new social contract based not on economic growth alone, but on social rights. Such a development would threaten the regime's founding asymmetry: that of centralised power, which grants without being constrained.

A second, more personal factor is worth highlighting. Xi Jinping has not been sparing in his criticism of the «Western-style» welfare state model, which he sees as "*likely to lead to moral decay, idleness and social disorder*"[8]. The influence of this vision is clear: when it comes to strengthening social security, the stated aim is above all to "*provide a safety net of last resort*"[9].

Finally, the construction of a welfare state is in tension with China's geopolitical ambitions. The logic of competition with the United States is pushing the regime to favour policies focused on production, exports and technological innovation, to the detriment of social investments deemed less strategic.

In fact, the advent of a welfare state close to European standards will remain unlikely as long as Beijing considers that extending social protection risks diluting the authority of the regime, or diverting part of the economy from security and technological objectives.

V • Domestic consumption versus technological ambition

At the same time as boosting consumption, China has no intention of relaxing its efforts in terms of industrial innovation. The country, which has closed the gap with Europe and the United States in several critical areas[10] thanks to the ten-year "Made in China 2025" plan and the power of state subsidies, is now focusing on public-private partnerships. The government has announced the creation of a national guidance fund for venture capital, capable of attracting $138 billion (€124 billion) in investment over 20 years. The aim is to support strategic sectors such as artificial intelligence, quantum technologies and robotics.

These policies serve the desire to reduce dependence on foreign markets - particularly in the face of protectionist measures from Washington - and to consolidate China's technological leadership. In the long term, an enlarged domestic market could compensate for the fall in exports, while mastery of high technology remains a pillar of Chinese autonomy in the face of American pressure.

VI • Persistent contradictions

Despite these major announcements, several paradoxes remain. On the one hand, the resources actually allocated to pro-consumer policies fall short of the expectations of Western analysts, who were hoping for more massive spending. Secondly, the question of funding has still not been resolved: local governments, strangled by their debts, are struggling to increase aid.

However, the trade-off between supporting consumption and supporting high-tech companies remains a delicate one. The recent

7 On 13 November 2024, a 63-year-old man killed 35 people in Zhuhai in a car bombing, https://www.theguardian.com/world/2024/nov/13/china-zhuhai-car-crash-tragedy-death-toll-sports-centre

8 "坚决防止落入"福利主义"养懒汉的陷阱" See article by President Xi Jinping in the 20th issue of Qiushi magazine, https://www.cls.cn/detail/852906

9 The accepted expression is "兜底" "support the bottom", so measures only as a last resort to avoid protest movements by citizens who have nothing left to lose, a long way from minimum social benefits such as the minimum wage.

10 Every year, the Australian think-tank ASPI publishes its *technology track record*, which shows that in 2024 China will dominate research in 57 of the 64 breakthrough technologies. The United States is first in the other 7 and second in the vast majority of the others, https://www.aspi.org.au/report/aspis-two-decade-critical-technology-tracker

example of DeepSeek, a pioneering start-up in artificial intelligence, illustrates this dilemma: encouraging production to win the "battle of the technologies" may exacerbate overcapacity in certain sectors, while on the other hand, boosting consumption does not offer immediate benefits for cutting-edge innovation.

VII • The reorientation of the Chinese economy is an opportunity for Europe

For Europe, greater trade cooperation with China offers an opportunity for diversification: the abrupt rise in US tariffs (10% for 90 days, potentially more depending on President Trump mood[11]) is driving the EU to seek new outlets. What's more, access to Chinese innovation is crucial if we are to stay in the global technological race and act as a bridge to a world that will be decoupling from the United States.

Conversely, China, which have faced a de facto embargo for a month, harming the bilateral trade must compensate for the loss of access to the American market by strengthening its trade partnership with Europe[12]. While taking care not to become a dumping ground for low-priced Chinese products, Europe can take advantage of the need for Chinese overcapacity to be absorbed by the European market, for example in the field of electric vehicles, via Sino-European joint ventures by supporting several conditions: 1) that the construction of these cars benefits European jobs and 2) that European manufacturers can benefit from Chinese technological know-how.

VIII • How can a fresh start be made to EU-China trade relations?

Europe must encourage the Chinese economy to develop its consumption, as this is the only sector that could absorb most of the industrial overcapacity and offer additional outlets for European companies (health, distribution, ecological transition, etc.).

The key to a fresh start could lie in negotiating a new agreement on investment. The CAI concluded in 2020 but never ratified is a good base for bilateral investment but is now outdated. The European Union could then make the entry of Chinese capital into its single market conditional on compliance with its standards (Clean Industrial Act[13], action plan for the automotive industry, etc.). A window of opportunity has opened, where China, which is very keen to increase its investment in Europe, could accept greater reciprocity in opening up its market to European investment, which has been in sharp decline for the past 10 years.

This new negotiated framework would encourage the growth of Chinese consumption by promoting goods and services with higher added value. Sectors hitherto poorly regulated in the initial agreement, such as electric vehicles, artificial intelligence and cyber security, could be subject to stricter requirements to ensure fair competition. Finally, by supporting more joint ventures between European and Chinese players in the electric car and other strategic sectors, we would be laying the foundations for a "win-win" partnership - where Europe would benefit from Chinese innovation and China would be able to move its industry upmarket.

11 https://apnews.com/article/donald-trump-trade-tariffs-european-union-f335ba9aa9d0b36cfe483f6f045c9b01

12 See Xi Jinping's statement with Spanish Prime Minister Pedro Sanchez encouraging Europeans to "team up against Trump bullying" https://www.theguardian.com/us-news/2025/apr/11/macron-speaks-of-90-days-of-uncertainty-as-trump-tariffs-spark-further-losses

13 See the European Commission website, https://commission.europa.eu/topics/eu-competitiveness/clean-industrial-deal_en

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