House of Commons

Business and Trade Committee

Oral evidence: China and the UK economy, HC 124

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Watch the meeting

Members present: Liam Byrne (Chair); Dan Aldridge; John Cooper; Alison Griffiths; Justin Madders; Charlie Maynard; Mr Joshua Reynolds.

Questions 138 to 172

Witnesses

II: Sam Olsen, Chief Analyst, Sibylline; Grzegorz Stec, Head of Brussels Office and Senior Analyst, Mercator Institute for China Studies; Andrew Small, Asia Programme Director, European Council on Foreign Relations; Professor Laura Murphy, Professor of Human Rights and Contemporary Slavery, Helena Kennedy Centre for International Justice, Sheffield Hallam University.

Examination of witnesses

Witnesses: Sam Olsen, Grzegorz Stec, Andrew Small and Professor Laura Murphy.

Q138 **Chair:** Welcome to today's second panel on the UK-China relationship. Thank you very much indeed to our witnesses for joining us. Laura Murphy, if I may, I will start with you. Just give us a sense and help us set the stage. What is the coercion risk to the UK from China?

Professor Murphy: I study forced labour in China in particular. One risk that does not get enough airtime is that holding industries captive in China means that they hold our values captive as well. If China owns the solar industry and the EV industry, it can then do whatever it wants all along the value chain, whether it is the subsidies we were talking about earlier, tax incentives, lack of environmental standards, or even forced labour. It can do all those things with impunity because we believe we cannot pull ourselves out of those supply chains.

When they turn to gross human rights violations, we throw our hands up and say, "There is nothing we can really do about the workers who produce the goods we consume, eat, wear and drive. We cannot do anything because all of our supply chains are there". That captivity means a level of coercion that goes deep to the roots of our democracies, values and due diligence. It means that our corporations become complicit in those violations of the planet and the people on it. That is a price that is too high to pay.

Q139 **Chair:** We are going to loop back into your personal experience a little bit later on in the questioning. Grzegorz, let me just come to you to help round out that picture. Give us a sense of what you see as the coercion risks to the UK from the economic relationship with China.

Grzegorz Stec: Relating slightly to the work that we have been doing in the context of the resilience audit, when we were mapping how 11 countries across Europe are specifically reacting to vulnerabilities and resilience vis-à-vis China, the UK really stands out on a few of those issues. First, with its lax FDI screening, the threshold for mandatory notification remains relatively low. Also, the reference to 17 specific critical sectors remains an issue compared to some other European countries that have more stringent FDI screening.

There is also the question of Chinese investments in the UK, which are by far the highest in terms of the volume across Europe. We are talking here about around an aggregate of €85 billion since 2020. This is more than investment from China in Germany, France, Spain and Poland combined in terms of value.

There is also the issue of UK investment in Hong Kong, where the UK is even more exposed than Germany. If we take Hong Kong jointly with China, UK investment in China and Hong Kong is still higher than German investments across the board. It is a similar story when it comes to exports. Research security also remains a key concern.

Q140 **Chair:** What are the threats, risks, dangers and perils to the UK from this level of economic relationship?

Grzegorz Stec: Of course, it is the question of pressure that is going to come, and the potential levers that China has vis-à-vis the UK and other European countries. If we take a look at the critical supply chains, this is the issue that touches all of us. Here, we are talking not only about the question of critical minerals and magnets across the board. The big picture issue is that China has the instruments to put pressure on us, which will make it harder for us to limit this dependence over an extended period.

If we take a look at the economic security toolbox that China is building, compared with what we are doing in Europe, where we are focusing on "partner, promote, protect", China also has a very considerable "punish" aspect of the measures that it is putting in place, so it can weaponise that.

Q141 **Chair:** I just want to really drill into this for a second if you do not mind. We are under pressure from all kinds of partners and non-partners from around the world. What are the bad decisions that we might end up taking because of this pressure? What are the things that we as politicians should fear this path leads to?

Grzegorz Stec: First of all, if you want to really boil it down to very concrete impact, it can be the job losses. The discussion that we also had in the previous panel is largely about the deindustrialisation of Europe and the job losses that we are seeing. This is part of the fact that the Chinese economic model is being built with control over future technologies in mind. Also, it is basically an export-led model, so the overcapacities are overflowing our markets, making it hard for us to really make our economies grow.

Q142 **Chair:** There is a loss of livelihoods there, and a loss of control and agency about the future.

Grzegorz Stec: Indeed, those are the key issues, but then there is also the aspect of the tools that this gives to the Communist party, because we have to think broader than just China and in terms of the agency of the party exercising political control. There is a possibility and, indeed, already a precedent of China using those economic leverages as a means of political pressure on certain countries. We leave ourselves exposed to the situation in which China may basically put pressure on Europe, whether that is the UK or other actors, in order to achieve other political goals.

Q143 **Alison Griffiths:** This is particularly for Professor Murphy and Sam Olsen. I am really interested in which sectors of the UK economy you feel are most dependent on Chinese suppliers.

Professor Murphy: As I have mentioned, the work that I do is particular to one region of China, but it is indicative of what China is investing in overall. It is investing in electric vehicles and all kinds of automotive, which is an industry that is of concern in the UK.

It is also expanding by the minute in steel production; there is a massive expansion there. There is a massive expansion in solar and all critical minerals. It is about both the competition against the products that are manufactured in the UK, and the raw materials that are necessary to that manufacturing. All of that is being systematically invested in through the central Government and local governments. All those things are also being made in Xinjiang, in the region where there is massive state-imposed forced labour.

Sam Olsen: It is really important to note that China is trying to create a number of levers over different types of industry in the UK and different types of economic activity. This is a concept we developed for the Foreign Office a few years ago that is called "structural influence", which is where a country builds levers of influence over another country in order to have that hanging in the air and to bend that country to its will.

Structural influence is a really important concept because China has built out structural influence over the UK and many countries in the world in a number of different sectors. This is important because the more that countries have structural influence from China, the more that they bend to its will automatically. They self-select on this. This means that, as China builds out its structural influence in sector A, B or C, you realise that you do not want to annoy it because you do not want to lose sector A, B or C. This means that, as countries, they basically bend themselves to China's will. We have so much evidence of this. That is the context.

Specifically on where we are here, it is absolutely clear. If you go through all the critical minerals and rare earths, that is just one element, but there are also the industrial components and all the advanced manufacturing. Remember that about one-third of the world's industrial capacity is Chinese, which is more than Britain, America, France and Germany combined. Because of that, it can go through every single one of our sectors and bend us to its will if it has the leverage over it.

This is incredibly important in two specific areas that I would say need to be highlighted. One is defence, and one is the renewable energy transition. It is no exaggeration. Our research shows this clearly.

Q144 **Chair:** Just unpack that a bit. Say a little bit more about what you mean by those two sectors and the structural influence therein.

Sam Olsen: Basically, the structural influence that China has over industrial supply chains in Britain, especially in the regions of critical minerals and other advanced components, means that it is now structurally and functionally impossible for Britain to rearm or to continue with the energy transition without Beijing's acquiescence.

Q145 **Charlie Maynard:** You mentioned economic security toolboxes. Let us be imaginative here. We have a big problem. There are some actions being taken. Let us say that in five years' time we have got our act together and moved quickly. Who would like to have a crack at what needs to change and what that would look like? Let us be optimistic here. We may not need to be, but let us try. What is at the top of that shopping list?

Sam Olsen: First, you need to map out the dependencies. We do not understand where our supply chain and economic coercion dependencies are at the moment. I used to be in the Army. I spend a lot of time with the MoD. They do not have a list of what we need to work on.

Q146 **Chair:** Is that still true? That is an extraordinary statement.

Sam Olsen: Yes, it is.

Q147 **Chair:** After years of debating this and agonising about it, you are telling us that we still do not know where the interdependencies are.

Sam Olsen: Yes. It is not just tier 1; it is also tier 2. For example, a lot of our uniforms are made in Cambodia, which in a sense is great because we are not making them in China, except for the fact that China has structural influence over Cambodia to the extent that two-thirds of Cambodia's exports come from garments and two-thirds of the inputs into Cambodia's garment industry come from China. That means China can turn off our uniform supply by putting structural influence pressure on Cambodia not to export to us. That is a tier 2 level of exposure.

We do not have a proper tier 1 or tier 2, let alone tier 3, understanding of where China has—

Q148 **Chair:** DBT tells us that it is in the process of setting up a supply chain centre to map and monitor all of this. Are you saying that it is not quite where it needs to be?

Sam Olsen: No. I do not know where they are on that, but it is not ready right now.

That brings us on to the second point. Once you have identified those critical exposures, you need to work out how to solve them. I will give you a quick example: copper refining. Copper is absolutely vital to the UK, to any industry. About half of all copper refining is done by China. If you look at the UK, we cannot push back on Chinese copper refining power. They set the market rate. A couple of years ago, Chinese copper producers said, "We are going to drop the market price", and they did. That puts a lot of stress on the west.

We did the research. If you go through an ally-shoring approach on that, you get together the NATO countries plus the IP4 of Japan, South Korea, Australia and New Zealand, and you bring those together as a group, that amounts to about 19% of global copper refining, which gives us enough leverage to push back.

The final thing that I will say is that, when we are looking at pushing back on China, we have to look at having a middle powers—or at least an interest-led—grouping, rather than just relying on the EU. The EU does not have all the things we need. The EU would not be able to push back on Chinese copper production, for example. Working with Japan and Canada, we can. That is the answer.

Chair: Andrew Small, what is your answer? Do you want to restate your question, Mr Maynard?

Q149 **Charlie Maynard:** What is in that economic toolbox and how do we get there? How do we use those tools? How do we develop those tools?

Andrew Small: You have already covered a whole range of different areas in part. One of them is the club-building piece, which has been hinted at. This is partly club building for the sectors at the highest levels of dependence, so the critical minerals piece, APIs and some other areas that people are trying to fast track at the moment. That club contains some of the countries that we have mentioned. There are pieces of this that you can do with the United States, as we see on critical minerals. There are other pieces where that has become more complicated and we are having to do it with a slightly different constellation of actors. Quite a bit of work has been done at the G7 in some of these areas already, such as legacy semiconductors. There are a number of these pieces.

You pretty much need to pick a range of strategic sectors that you care about most and build ex-China scale and capacity. You can get to that in different ways. You have to be able to defend those sectors in certain ways. This means aligning the tools on trade defence and consumer subsidies. It means procurement decisions. You basically have to align a number of those decisions across a range of the key economies.

Q150 **Chair:** Sorry, slow down. Just go through that list again. You mentioned procurement decisions and you said a couple of things before that.

Andrew Small: It is about procurement decisions and consumer subsidy decisions. Across the clean tech sector, if you align consumer subsidy decisions across France, Germany, UK and Japan—we have already had it in the US—the market scale that you are able to build on this is significant. In France, for instance, when some of the most effective subsidy schemes were brought in, you had a collapse in Chinese electric vehicle market share from around 30% to 4% within a few months.

You can get at some of these things with clever deployment of these schemes, but they need to be aligned. This is why the Ming Yang decision, for instance, was such a critical one. This is the sort of decision that has implications for the entirety of the European wind industry. It is not just a classic security-related decision. The alignment of these sorts of decisions decides whether we are able to keep these industries at all.

First is indeed to be able to identify the industries and sectors that we care about most and the dependencies we are most worried about. We then need to mobilise at scale between a number of these economies. These tools that I mentioned are the market-based tools, but a lot of these are going to be security-related tools as well.

Q151 **Charlie Maynard:** Can I just jump in? With the WTO appellate body being effectively defunct, what is the solution to replace that? That has been the biggest tool that we have had over the last 30 or 40 years, but it is now completely dead. Is anyone doing the running as to how to replace that?

Andrew Small: The WTO would have worked with China in the 2000s and worked less and less with it in the 2010s. It was non-functional as a way of dealing with any of these issues with China in the 2020s, probably even by the mid-2010s. It adheres to some of the decisions, but no fully multilateral structure is going to address this. This is going to have to be through plurilateral frameworks.

Q152 **Chair:** Is the implication that we should just call time on the WTO now? We have just gone through an enormous list of things that skew the playing field. It is obvious that we are not going to remedy much of this through WTO structures. Are we deluding ourselves by continuing to think that we can fix this through the WTO?

Andrew Small: It is a lower priority in the scheme of how you would go about addressing this. A substantial portion of trade will continue to be conducted under WTO rules. A substantial portion of trade with China can continue to be conducted relatively safely. In a sense, this is what is being negotiated even between the US and China at the moment. You are picking a series of sectors that you are not worried about and where you are not concerned about what these dependencies amount to, and figuring out some kind of managed trade framework for dealing with these things.

However, if you align cyber rules across a number of the key economies, you pretty much ex-out China from a number of these sectors. That includes, for instance, the entirety of the connected sectors, such as 5G, inverters or connected vehicles. You can go down the full list of these things. There are more and more sectors that are connected sectors, of course. The rules that one has in place for over-the-air updates or data effectively force Chinese entities either to create monitorable facilities outside the country or to be ruled out of some of these markets entirely.

In terms of alignment on that, we have seen some movement on the EU side with the revisions to the Cybersecurity Act. In a few years' time, which is the timeframe that you are talking about, we should have what are effectively much more rigorous product safety rules across a lot of sectors in ways that would mirror what we have already seen with 5G. The US has moved on connected vehicles and a number of these other areas.

This is the other way that you get to market scale. You need to have some sectors where you make a decision that says, "On safety and security grounds, Chinese products are going to be excluded" and have some cross-cutting rules that apply there.

Grzegorz Stec: To add to those great points, which I agree with, we have to assume that China will counteract any actions that we take in that space. We should not base it on the assumption of a passive China. Beijing has been building this economic security toolbox in order to use it, and has already been using it. In that context, any form of resilience also needs to take into account building up our deterrence capacity, which needs to be a group one.

There are three points on this. First, gathering information about our exposure and our companies' exposure to China is a necessity. We are not there yet. To a large extent, Beijing is requiring companies to disclose their entire supply chains as part of licensing. The companies have to prepare this information anyway. The fact that we request it to be available to our own Governments would definitely be one of the moves to close the information gap that we have with China.

The second part is really related to the tools, in my mind. In that context, the work that is being done in the UK right now, the conversation related to adverse economic pressure powers, is critical. Within the EU, the anti-coercion instrument is an equivalent of that, but it has its own problems.

That leads me to the third point. Even if we have those tools, we align the deployment of them, we use them and we create any sort of economic NATO, any sort of anti-coercion coalition, there is still a question of political will. This is a takeaway from our resilience audit exercise. A lot of countries across the EU have put in place a number of measures related to FDI screening, but they just do not use them vis-à-vis China, given the lack of political will and similarly—this is something that China sees—the pain threshold gap between us and China. Our societies are deemed by Beijing to be simply not willing to take the heat of economic struggle. If we are going to back down, Beijing feels like it is in a position ultimately to dictate the rules of the game when push comes to shove.

Once we start putting in place measures that can really threaten things for China, Beijing is going to respond. We see that to a certain extent, for example, in the context of the Industrial Accelerator Act. There is some signalling of a push on this and we are going to see how it evolves in terms of the pressure that China will put on the EU.

The deterrence component, to my mind, is absolutely critical because it allows us to buy time for all those other measures that are absolutely vital to kick into place and to bring the results that we would hope for.

Q153 **Chair:** Laura, can I ask you to bring in your own experience of the university sector, which we know is especially exposed to Chinese students?

Professor Murphy: I will also answer the previous question briefly as well, if I may. I believe that some kind of critical minerals marketplace with allied nations is essential. It is being developed by many different countries right now. They are thinking about how to make it work. Now is the time to get in on that.

Subsidies and incentives for the expansion of green technology manufacturing in the UK are not only essential but doable. It takes 18 months to get an ingot and a wafer factory put up in a country. It is absolutely affordable. It is doable. It provides jobs. It provides you energy security here in your own manufacturing backyard. It is also not polluting, so, hey, it is a win for everybody, right?

On top of that, the university system is an important aspect of this. Investing in innovation is critical. When we see market distortions such as forced labour, lack of environmental standards or massive subsidies going on in China, the price drops on the goods that are exported from China, leading to an inability to spend any money on innovating for new technologies outside of China. China then ends up holding that technology captive. It did this with polysilicon. There are other technologies for solar manufacturing that have been dustbinned because nobody can afford to continue with the innovation. That is where Governments have to come in and help with that innovation, assist universities in doing that work and assist companies in doing the manufacturing.

A forced labour import ban, absolutely in collaboration with subsidies in the US, helped to move industry back to the US, including in solar but also in textiles and other industries that were held captive by China. When they said, "Okay, we are not going to buy goods that are made with forced labour and let them come into the United States", that provided an incentive for higher-priced goods, yes, and for employment in the United States to grow. Solar industry companies had been closing and now they are on the upswing. That is due to both IRA subsidies and the forced labour import ban.

Q154 **Chair:** Before I bring Mr Madders back in, just give us two minutes on the experience that you went through. It is a good case study of how these coercion dynamics can unfold.

Professor Murphy: This is the work that I do. I work specifically on forced labour and human rights violations in China. We published a series of reports that outlined the supply chains that were connected to that. I suppose the Chinese Government found that to be threatening enough, as Sam was saying, that they came to my university, and since 2022 they have been telling my university, Sheffield Hallam University, to silence me and end my research.

For years, the university stood by my academic freedom and said that it would back me. In 2024, the Chinese Government began to do a multi-pronged attack on the university. We had a lawsuit from one of the companies that we investigated. We had cybersecurity attacks. Our staff on the ground in China were interrogated. Messages were sent directly to my university to silence me. The university's website was taken down from being accessible in China, limiting the number of students to the university. The university decided to choose the student market over my academic freedom.

We can see that the Chinese Government simply do not stop. We had a little bit of bad social media coming from them. We had a little news story and a press conference in the early days. As our work gained more prominence and more influence, and, admittedly, as I joined the US Government in working on this issue, the Chinese Government increased their pressure. They knew that my employer was the greatest lever to silence me.

Q155 **Chair:** What did the UK Government do to defend your academic freedom in the conversations that they had with Sheffield Hallam?

Professor Murphy: In fact, despite my repeated pleas to the university to go to the UK Government for help, it refused to get any assistance. For a long time, the UK Government had no idea that this was going on. When they were alerted to this, they came to me and provided me with some assistance and some support, but they also approached the university. Apparently, they approached each other at the same time. It is a matter of debate these days. It was a year into this trouble that the UK Government stepped in.

In the last several months since my story became public, the Department for Education has really swung into high gear. It has put £3 million behind a foreign interference programme. It has had vice-chancellors in to tell them what to do. It has a new hotline for vice-chancellors and administrators. The Office for Students has created a hotline for people like me. It does look like the needle is moving, but it should not take someone coming forward like I did.

Q156 **Chair:** What lessons do you learn from this unhappy episode?

Professor Murphy: My biggest fear for the university is that the biggest lesson that it learned was not to put things like this in writing any more, rather than not to do it.

Chair: What a good lesson.

Professor Murphy: I fear that the real lesson it will learn is not to talk about it.

For me, one of the biggest lessons is that I was able to come forward because I have a great deal of privilege. My job is secure. My family is not in China, although some of my researchers' families were. I had lawyers who were willing to support me. Most people do not have that. Most people who are being threatened by the Chinese Government or by their own universities or employers do not speak out. We have to have avenues through which people can hold universities accountable and through which they can receive support. They really need that government support.

Chair: Mr Madders, thank you for your patience.

Q157 **Justin Madders:** Greg, could I just go back to the dilemma around what I would characterise as how far you push on these issues to untangle yourself? The point that you are making is that China is not going to be passive in this. Does this need a concerted political drive over a long period? Is there a point at which—we may have reached it or we may be going to reach it shortly; I do not know—the pain will be too much and we are too far in? Is there any way of getting a sense as to whether anyone is actually thinking about that?

Grzegorz Stec: Maybe one point on this is a quote from President Xi Jinping from 2023: "If we pursue economic development through struggle, we will succeed. If we pursue it through concession and weakness, we will fail". This is the mindset that China is currently in, in the context of building the entire toolbox.

There is going to be substantial pressure from the Chinese side once we reach the issues that are really vital for the Chinese Government. Part of the issue is that those red lines have been moving over the last years. Basically every time it is going to be a case-by-case basis, to a certain extent.

It is really important to acknowledge that there is a need to build the political will to struggle, to a certain extent, in Europe. There are going to be pushbacks. It is also important to impress on the public that, in this context, there are no pain-free solutions. It is just a matter of what type of pain we choose and whether we choose it on our own terms and in the context of specific prepared moments or whether it is going to be selected by China.

Sam Olsen: I am quite optimistic that there are very good options for the UK, if we get it right. Maybe the future is not as painful as we think. First, we have to understand that the fourth industrial revolution, and winning the fourth industrial revolution, is absolutely the centre part of China's strategy. That fourth industrial revolution is networked. It is driven by AI, but it is bringing robots and everything together in a way that is absolutely linked. China wants to create this fourth industrial revolution network where we basically become part of it and therefore absolutely surrender our sovereignty to that platform moving forward.

However, if we realise that we can work with other countries—Japan, Australia and Germany, etc—and we push back and create some kind of alternative centre of economic and political gravity, we have the innovation, the industrial capabilities and the technology to combine and move forward in a way that is going to generate huge benefits for the UK and our allies. It has got to the stage now where, if we do not make a decision in the next few years, we will have a very simple choice of direction: to be linked to Chinese platforms for a long, long time or to make our own destiny come true with all the benefits that that has.

Chair: I would agree with that.

Q158 **John Cooper:** Mr Small, I wonder whether I could come to you and ask about the situation in Taiwan. I was in Taiwan and the People's Liberation Army was just across the way, exercising what clearly was an invasion of Taiwan, which concentrates the mind. Across the South China sea, the Chinese are building islands that are designed to push back the American Seventh Fleet. If it was all to kick off there, would we be affected? It is the other side of the world, but should we be worried?

Andrew Small: The immediate economic shock effect for the UK, for Europe and anyone else would still dwarf any of the economic shock experiences that we have gone through with the global financial crisis or Ukraine. You have to start adding them on top of each other before you can get there. That is in the limited scenarios. That is in the really minimal scenarios that we are talking about, where we do not see spill-overs from a military invasion of Taiwan into, for instance, other theatres. It is highly probable that it would spill over into other theatres.

We are talking about multi-trillion-dollar shocks. They ripple out. The immediate neighbourhood gets hit hardest, but Europe is proportionately hit even harder than the United States. The UK is hit at about the same level as most of the other European countries. You get an immediate economic shock effect on that sort of scale. Most of the transmission mechanism for this is the cut-off in advanced semiconductor supply, which has the convulsive shock.

Q159 **John Cooper:** On that point about semiconductors, the Taiwanese talk about the silicon shield. They regard their ability with chips as something that protects them. Equally, we are told that 2027 is a possible date for invasion. What is the likelihood of something like this happening in the next decade?

Andrew Small: There are some dates to watch for. First of all, you have the Taiwanese elections, which are quite pivotal. Going into these elections, China still thinks it has the scope to influence the political outcome in a way that is favourable. As we are seeing even in recent days, the direction is to squeeze the DPP, squeeze Lai, create a situation in which a friendlier KMT Government come into office and then reach a political solution, which would be a coerced solution.

Q160 **John Cooper:** Do the Chinese think that they can win without fighting?

Andrew Small: They think they can for now. The question is what happens if they fail in this strategy. Here is the problem. You get a really high window of risk towards the end of the decade, particularly if you look at the period from 2028 to 2030. You have this period in which PLA capabilities deployed in the region will almost certainly have an edge over US-deployed capabilities at the time. Some of the US systems will only come online in the early 2030s. If we look at the munitions depletion in Iran, that imbalance has worsened further.

You could see a risk window through this period, in which China may calculate that its political strategy has failed and it does not want to pursue a military strategy ideally, but there is an opportunity window for it that may close. Of course, there may also be a political opportunity window that relates to the way the United States approaches this question, which is the crux for China. Can you create a set of political conditions in which the US is unwilling to intervene? Ideally, you create such uncertainty about the US willingness to intervene that you are again able to reach some kind of coerced political solution directly with Taiwan.

Q161 **John Cooper:** Are we prepared for this scenario? Is the UK ready to handle this? Are we simply unprepared? We seem to be talking about it and to be aware of dates, but are we doing much about it? Are we readying for this?

Andrew Small: I cannot presume to talk about everything that is going on in the UK Government, but the Taiwan scenario is one that has been, in certain ways, better prepared for and thought through, at least in terms of people going through and conducting their tabletop exercises, mapping out some of the scenarios and things like that.

Q162 **John Cooper:** That would only give us an indication of how bad things are going to be.

Andrew Small: We know how bad it would be. That is it. If we are then looking at the economic impact effects, the dependency risks and all these things, have we made significant progress on this in the last few years? No, obviously not. The dependency risks are worsening and the concentration of industrial capacity in China is growing.

The more that these monopoly levels of dependency on China grow, the more that the risks go up. It is precisely these kinds of plausible shock scenarios that we need to be ready for. Economically, I am not sure we are ready for what these impacts would look like. By "we", I mean pretty collectively. There is nothing that we have done over the last period, even when staring at this problem, that means we are in a much stronger position to mitigate this. There are some moves of advanced semiconductor manufacturing capabilities out of Taiwan, but, proportionately, we would be well into the 2030s before that would have a material consequence for the global economy.

Militarily, it is not completely clear that we are ready for this either. One of the greatest risks on this is precisely that we will have to deal with a cumulative set of cross-theatre scenarios at this time. We will have

Russia war risks in Europe and war scenarios on the Korean peninsula. In terms of NATO being able to do the kind of preparatory work that would be required for looking at two-theatre conflicts, that has just really not been done to a serious extent for various reasons.

Chair: On that happy note, we are going to accelerate.

Q163 **Mr Reynolds:** Sam, Make UK has reported that 49% of British exporting manufacturers have increased their UK sourcing over the last five years and 63% are intending to do so over the next five years. With that in mind, what measures are UK businesses and the Government taking to de-risk economic coercion from China?

Sam Olsen: It is a great question. The trouble is that there are not that many measures that they can take to properly de-China-fy, so to speak, simply because China produces a lot of things that we cannot.

I was talking recently to a middle-sized British defence company, which has now run out of rare earth magnets from China. Despite China saying that it was not going to throttle back on rare earth exports, it has definitely throttled back on rare earth exports. This company, which is an important provider to the Royal Navy, has basically run out. It is now working with American exported rare earth batteries, but they do not have the same performance.

It is really important for the British Government to say, "We know that there are things that can be done to improve the capability of British industry to survive against Chinese coercion", but British companies working on their own are really in a bad place because they just do not have the tools or the capabilities.

Q164 **Mr Reynolds:** What things should the British Government be doing, then? Is it tax breaks or is it more than that?

Sam Olsen: First of all, it is setting the strategic direction. That is the most important thing. It is saying, "We understand that China has the ability to coerce. Therefore, we are going to try to find allies within these sectors".

Let us get that list of sectors. We did a really good job with AUKUS pillar 2 by saying, "These are the technology sectors that we are going to focus on. Let us build a ring of allied steel around those. Then how do we support British industry within that?" That is not just about working with allies; it is also about Government contracts. One of the big problems with defence SMEs is not being able to get Government contracts to leverage in order to get private finance.

The British Government have loads of little tools, but there needs to be a mentality switch. We need to recognise that we have moved away from a globalised world where we trust everyone into a post-globalised or re-globalised world where we need to choose our allies and work on a solution based around that.

Q165 **Mr Reynolds:** Finally from me on this, the CBI said in April that the UK must not cut itself off from China. The British Chamber of Commerce has warned that mixed messages from different branches of Government create a risk-averse environment in which China is often treated as high risk, which means we miss opportunities. What is your answer to those things?

Sam Olsen: There are three ways of looking at the UK-China economic partnership. No. 1 is through trade. That trade is overstated. The business community always goes on about how amazing China is. China does not need much of what we have to offer. That is why we only export £29 billion and we import £73 billion or something.

Secondly, even in the areas where we do have successful trade relationships, they are open to coercion, such as students and tourism. Do we really want to expose our businesses to that? There are lots of allied countries with which we want to have a better relationship. Every single time we do a trade delegation to China, it is a missed opportunity to do a trade delegation to Japan or Australia. Those countries want to be our friends and they are our allies. I really dispute the business community saying that there is a massive China prize because it is about opportunity cost.

Q166 **Charlie Maynard:** We have spent a lot of time talking about China's strengths and our weaknesses. What about the opposite? What are its weaknesses? How much time are you thinking about that? Do you have any particular ideas around that?

Chair: For example, it has to have access to the €10 trillion European consumer market for its model to sustain itself.

Andrew Small: It is in a more vulnerable period at the moment. There is this interesting combination of greater confidence and greater vulnerability at the same time. If you look at the economic situation in China, it is weak demand; it is weak housing market; it is weak consumer confidence; it is weak investor confidence; and it is deflation. It is pretty uniformly bleak-looking.

We know the headline numbers for GDP are borderline fictitious. Even those numbers do not look good when we keep seeing the new data coming out. There is a level of economic fragility that was not there before. The only significant growth driver has been either government spending and financing, in various ways, or exports.

Proportionately, it means that the Chinese economy is therefore more dependent on exports than it was during previous periods. At the same time, they have hardened their economy and, as Greg was talking about, they have put a model in place that means their coercive capabilities are much stronger.

They think they are in a weaker position in terms of being able to withstand certain forms of economic shock at the moment. Clearly, growing at 3%—or whatever number you think the real one is at the moment—leaves them in a more vulnerable position to the kind of major escalation that they saw with the United States. They want a period of relative peace at the moment.

They want to reach some settlements during the period in which they are navigating this phase. They know they have significant deficits in some areas. There are still a huge number of areas relating to advanced semiconductors that they need to bridge. The finance system is still extremely vulnerable to the dollar system. They are not much closer to getting that fixed in the next few years. They still need a lot of that external demand, which is precisely why they want to coerce countries to stay open.

Some of this is simply about the way that the Chinese system works. In a sense, we can choose how we wish to relate to this. This also goes to this tools question. They are very vulnerable to, for instance, transparency-related demands.

If you look at what has gone on with the first use of the new regulation that the Chinese put in place essentially to control the co-operation of Chinese firms with international supply chain regimes, one of the first points at which this was applied was in response to the EU foreign subsidies regulation's use of transparency demands for Nuctech. They have immediately responded by denying all co-operation with the EU side.

In some of these areas, the way that the Chinese system operates means that there are economic tools that we can use on our side as well that elicit, in some cases, even more dramatic responses than some of the trade defence measures, for instance. There are things that they do not want to—

Chair: We are running slightly out of time, so I am going to accelerate us through.

Q167 **Dan Aldridge:** Sam, if I can come to you, the Government have launched a consultation on potential powers to protect the UK from adverse economic pressure. You talked about a mentality switch, and I thought that was really interesting. Where should the balance lie between the need for consultation and scrutiny, and the need for a quick response on this?

Sam Olsen: China often characterises the west as being very good at process but not very good at delivery. We need to move more into realising that the world is absolutely prioritising delivery over process. There is a balance in that, but we need to move more quickly. The clock is ticking because every month we get more and more Chinese exports. These are platform-led exports. This means the world is being cut off.

As I would categorise it, the world is basically splitting into the 25%, which is the west and its close allies such as Japan, and the rest of the world. The rest of the world is increasingly coming under Chinese dominance around technology and industrial outputs.

You go back to where we can push back on China. That links very much to your question. Making it harder for China to go to the west and to build a bridge here is really going to push it down. We need to use that as a springboard and say to other countries around the world, "We are the ones who are standing up to China. Why don't you come and be part of our group?" It has got to that stage now.

Q168 **Justin Madders:** Professor Murphy, how are the Government doing in terms of eliminating forced labour from supply chains?

Professor Murphy: In the UK, they are not doing anything at all, really. Right now, you could bring a container ship into a UK port with a big sticker on the side that said, "Made with slave labour", and it would enter the market with no barriers. We have a little clause in a healthcare procurement Bill. We have a little clause in the Great British Energy Act. Otherwise, we have no protections. Consumers do not have protections to know that their goods are free of forced labour. Businesses do not have protections from the market distortions of forced labour. The Government have no explanation for how they are going to change that right now.

Right now is the moment when the UK really has to step up on this front. The United States has, for better and for worse, threatened economies around the world with tariffs if they do not create a forced labour import ban. That is not how I would have convinced people to do that, but it is hanging over everyone's heads. El Salvador has passed a forced labour import ban. Indonesia and Pakistan have passed bans in the last three months. Thirteen other countries have agreed to do it.

We know that right now the UK is not at risk of becoming a dumping ground for forced labour-made goods. It is a dumping ground for forced labour-made goods. Isotopic testing proves time and time again that stuff that is not going to the US because it banned the import of forced labour-made goods is coming into the UK. We really have to get on this now. If you do not, it is just going to mean that the world is closing in on ensuring that the UK receives all those goods.

Justin Madders: Thank you. That is very clear.

Q169 **Mr Reynolds:** Very quickly, the UK was at one point the world leader against forced labour.

Professor Murphy: Yes, in the 19th century and the 21st.

Q170 **Mr Reynolds:** What has gone wrong?

Professor Murphy: The Modern Slavery Act is nice enough. It was a good start. It was important that the UK kicked that off—most countries lagged on that front—but it does not actually have any teeth. It does not require companies even to report. They can report that they have done nothing this year—that satisfies the law. The vast majority of companies do not even do that. They could legit just say, "We knowingly import goods made with forced labour," and there would be no penalty for that.

Q171 **Mr Reynolds:** Do we need a new piece of legislation?

Professor Murphy: We need a new piece of legislation. It should include both a forced labour import ban and human rights and environmental due diligence. It could be two separate pieces of legislation. One of them ensures that companies know what is in their supply chains. The other one penalises them for bringing in things that are made with forced labour.

As I said before, that should be paired with subsidies to assist companies to manufacture those goods in the UK. That will bring jobs to the UK. It will help you to ensure that you are not going to be held captive to goods that are made in China.

Q172 **John Cooper:** Very quickly, Mr Small, I wonder whether I could come to you. We heard about American tariffs. Economic shots have been fired between the US and China, notwithstanding the recent visit by President Trump to China. Are we innocent bystanders in this war? Are we likely to get caught in the crossfire? Is there much we can do about that?

Andrew Small: There is a sort of truce at the moment, effectively. First of all, there is the agreement that was reached in Busan last year on rare earths. They are still restricted, but the more extreme measures that the Chinese side was proposing have still been held off for now. Of course, the US pulled the tariffs back, but it has also frozen quite a few of the economic security measures that it had been pursuing.

China essentially put the US on the back foot as a result of the way the entire thing was handled. The advantage of that is that it is, for now, a somewhat more stable framework than we had with all the volatility last year, where there were clear spill-over implications for everyone else from that level of escalation. There are downsides to the fact that the US is now not pursuing as robust an approach on a number of different areas, such as economic security, technology controls or even Taiwan. It is not necessarily that the equilibrium is conducive to the best outcome all round.

There is some expectation that for now the US does not want to embark on a major trade escalation. The fear that it has at the moment is that China has escalation dominance because it can essentially shut down the functioning of the US economy and a number of other economies. Because China also wants to maintain a relative period of peace while it builds out and addresses some of its deficiencies, there are some tentative reasons to think that this has a chance of holding for a time, even if it is extremely volatile.

Chair: We are out of time. That has been an extremely useful discussion. Thank you very much indeed. What we would really benefit from, if you were in the market for this, is some follow-up on something that Mr Maynard asked earlier. We would like to get your sense of where the vulnerabilities are and which tools we could be using. Mr Small, I know ECFR has published a short table of these tools, but we would really benefit from your advice on some of the other tools that we might equip ourselves with. That concludes this panel. Thank you very much indeed.