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Chinese economic influence as a potential security threat: The Dutch response

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Frans-Paul van der Putten – December 2022

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Summary

This Hybrid CoE Working Paper focuses on China's economic influence as a potential threat to national security and the government's response in the case of the Netherlands, one of China's largest economic partners in the EU. For the Netherlands, the main vulnerability stemming from economic interaction with China at present is that it can lead to strategic dependencies. The ongoing efforts of the government to increase Dutch economic resilience (and to do so together with the rest of the EU) seem to coincide, by and large, with heightened awareness that economic relations with China can have national security implications, and the EU's increasingly tense and complex relationship with China. The key issue that currently remains to be addressed by the Netherlands is how to develop a clear idea of China's economic importance. Economic resilience requires defensive security mechanisms as well as a strong economy. Under the current circumstances, a precise assessment is needed of the relationship between the risks and benefits of Dutch economic relations with China.

Introduction

In recent decades, China has developed into a major economic counterpart for many European countries, and for the European Union as a whole. This process started in the late 1970s with the opening up of the Chinese economy to foreign trade and investment, and accelerated after China joined the World Trade Organization in 2001. For many years, European governments favoured and actively promoted closer economic ties with China. However, in recent years this attitude has changed. European governments now view economic integration with China with increasing caution. While in most countries governments still aim for economic benefits, they perceive China's economic influence as potentially harmful to their national security or even as a source of hybrid threats.

This Working Paper is focused on China's economic influence as a potential threat to national security and the government's response in the case of the Netherlands,[1] one of China's largest economic partners in the EU. Being an open economy that is highly dependent on international trade, the Netherlands is potentially very vulnerable to foreign states that use economic influence for political purposes. This paper discusses the relevance of the notion of hybrid threats, describes the relationship between Chinese economic influence and national security, and traces the evolution of Dutch policies in the field of economic security. The concluding section discusses how current policies relate to the main potential vulnerabilities.

1 This paper was commissioned by Hybrid CoE in light of the more security-oriented approach taken by the Netherlands in recent years towards Chinese economic influence as a hybrid threat.

China as a source of hybrid threats

The concept of a hybrid threat generally refers to an action conducted by state or non-state actors whose goal is to undermine or harm a target by combining overt and covert military and non-military means.[2] When applied to China as a potential source of hybrid threats towards the Netherlands, the most relevant aspect of this concept is neither the combination of military and non-military means, nor of overt and covert actions. Military power or overt attacks do not play a significant role in China's approach to the Netherlands. Non-military means (derived from economic influence) and covert activities (cyberattacks) are far more relevant.

All in all, the notion of hybrid threats helps European governments detect differences between the approaches adopted by China and other states, particularly Russia, for whom the notion seems much more applicable. Moreover, it provides an analytical perspective that raises the question of whether, at a future stage, the Chinese government might switch from relying on non-military means and covert actions, as two largely separate areas, to a more integrated approach that also includes military coercion or deterrence, and overt measures that directly harm or undermine Dutch security. Finally, it points to the pertinence of a key issue: How can a European government distinguish between forms of Chinese economic influence that are aimed against their country's security interests, and instances of economic interaction that are beneficial or at least not intentionally harmful?

The Netherlands does not have a conceptual instrument to address the latter issue. Its main tool in this respect is the Dutch China Strategy, published in a 2019 policy paper,[3] in which the government noted that economic interaction with China involves both beneficial and potentially harmful aspects. Another conceptual tool is the EU's position on China, also published in 2019,[4] which views China as a combination of a partner, an economic competitor and a systemic rival. Neither the Dutch nor the EU statements have made it clear where they draw the line between unwanted and wanted forms of economic relations with China.

2 See https://www.hybridcoe.fi/hybrid-threats/. Hybrid CoE's definition of hybrid threats does not make a distinction between legal and illegal tools. Nor does the definition used by the Dutch government: hybrid threats are defined as threats resulting from 'states acting as being in a state of conflict, largely below the legal threshold of an openly armed conflict, with an integral deployment of means and actors, and having as their aim to achieve certain strategic goals': NCTV, 'Chimaira: Een duiding van het fenomeen "hybride dreiging"', April 2019, 6, https://www.nctv.nl/documenten/rapporten/2019/04/18/duiding-fenomeen-hybride-dreiging. [All links were last accessed on 8 November 2022, unless otherwise indicated.]

3 Netherlands Ministry of Foreign Affairs, 'Nederland-China: Een nieuwe balans', May 2019, https://open-pilot.overheid.nl/repository/ronl-bcdd2998-edb5-4c17-bb1b-876f10a5ed45/1/pdf/Samenvatting%20China%20versie%2015%20mei%202019.pdf.

4 European Commission, 'EU-China: A strategic outlook', 12 March, 2019, https://ec.europa.eu/info/sites/default/files/communication-eu-china-a-strategic-outlook.pdf.

Dutch national security and Chinese economic influence

Five questions need to be addressed in order to understand how China's economic influence relates to Dutch national security. First, is there a conflict between China's foreign policy aims and Dutch national interests? The Chinese government has a number of main aims that are not compatible with Dutch interests, or compatible only in a limited way: strengthening China's economy at the expense of the competitiveness of other industrialised nations; expanding China's global influence while limiting the influence of Western countries; and detaching the norms of international relations from their underlying liberal values.[5] None of these aims are directly targeted at the Netherlands or at Dutch national security. However, since the Netherlands is an industrialised state, part of the 'West' (a US-led group of countries with close economic, diplomatic and military ties), and benefits substantially from international norms based on liberal and democratic values, China's foreign policy potentially undermines Dutch interests.

Second, how might the Chinese government use its country's economic influence in ways that are aimed at undermining or harming Dutch security? The main concern from a Dutch national perspective is that China could use its economic influence for political leverage that would weaken Dutch (or the EU's) sovereignty. Another concern is that in the event of a military confrontation between China and the US, the Chinese government could use its economic influence to inflict damage, by way of sabotage, on US allies such as the Netherlands. A further concern is that China could use economic interaction as a way to steal or compromise information that is related to Dutch security, or to erode the competitiveness of the Dutch economy.

Third, what is the potential for China to use economic influence for political leverage? For some individual Dutch companies, China is a strategically important market, investor, or source of industrial products, technology and talent. Particularly in the case of companies active in advanced technological fields, such as semiconductor manufacturing, the economic relationship with China may be of great consequence. Still, at first sight the economic importance of China for the Netherlands at the overall level may seem limited. As far as the Netherlands is concerned, China is not among the largest direct investors, export or investment destinations, and nor is it a top trade partner in services. China is only a major partner in terms of imported goods (the second largest after Germany), accounting for 10% of all imported goods in 2021.[6] However, more importantly, China is Germany's largest partner in terms of traded goods.[7] Since Germany is the main destination for Dutch exports, and the Netherlands is the second-largest source of German imports (behind China but ahead of

5 Assessment of Chinese aims based on an analysis of the evolution of China's behaviour in international affairs since the late nineteenth century: Frans-Paul van der Putten, *De Wederopstanding van China: Van prooi tot wereldmacht* (Amsterdam: Prometheus, 2020), 258–269. Specifically on Chinese norms versus liberal values: Van der Putten, 'Harmony with Diversity: China's Preferred World Order and Weakening Western Influence in the Developing World', *Global Policy*, Volume 4, Issue 1 (February 2013).

6 See https://longreads.cbs.nl/nederland-handelsland-2022/internationale-handel-in-goederen-samenstelling-en-geografie/.

7 See https://www.destatis.de/DE/Themen/Wirtschaft/Aussenhandel/handelspartner-jahr.html;jsessionid=06F60CEBD5A1412A2092DBF44A975ED8.live722.

the US), it may be assumed that many Dutch exports are indirectly linked to Germany's China trade. This means that China's potential leverage in the economic domain is largely Germany-related.

On the one hand, some Dutch sectors are potentially exposed to Chinese pressure. This applies to companies that act as suppliers for German exporters, such as those in the automotive industry, and logistics firms that support German foreign trade, especially related to the port of Rotterdam and Schiphol Airport in Amsterdam. The port of Rotterdam in particular, being Europe's largest seaport, plays a key role in the Dutch economy. The main actor in container terminal management in Rotterdam is Hutchison Port Holdings, a Hong Kong based company. Two Chinese state-owned enterprises, COSCO and China Merchants, have minority shares in container terminals in Rotterdam (as well as stakes in many other European ports). Moreover, China is a major source of and destination for containers handled at Rotterdam, and COSCO is among the most influential container carriers globally. As a consequence, the port sector is a major focal point for the Netherlands when it comes to assessing the relevance of China for critical infrastructure. On the other hand, these sectors are to a significant degree shielded from direct exposure to China since Germany is the linking factor. Nevertheless, there would probably be considerable economic consequences if the Netherlands were to lose its prominent role in Sino-German trade.

The context within which dependencies exist should also be considered. It matters a great deal whether or not China relies on the Netherlands or the EU for strategic dependencies. The greater China's own dependencies relative to those of the Netherlands, the less leverage the Chinese government has. For China, the Netherlands is strategically important as a transport hub for trade with Germany and as a source of chipmaking equipment (a large manufacturer of which is ASML, a Dutch company). Moreover, the EU as a whole has great strategic significance as an export market and as a source of technology. These factors have a moderating effect on the possible political leverage that China derives from its economic ties with the Netherlands.

Prospects for the future are also relevant when it comes to China's ability to leverage its economic ties with the Netherlands. As EU-China relations become more tense, and Germany increasingly views China as a competitor rather than a customer, in the coming years Germany's foreign trade could potentially diversify away from China. This would mean that the Netherlands would likewise become less dependent on China. On the other hand, China may become a dominant economic actor in the developing world. Weakened economic ties with Western countries would further induce Chinese companies to focus their international strategies on Asia, Africa and Latin America. Since 2013, the Chinese government has been developing the Belt and Road Initiative (BRI) as a policy framework for economic expansion in developing countries (and in the EU), which will probably continue to be a main pillar under China's relations with the developing world. Insofar as German companies and their Dutch suppliers in the coming years and decades might redirect their attention away from China to other countries, they are likely to still have to engage with Chinese counterparts. For now, the Netherlands duly needs to take into account the likelihood that China will remain an influential economic actor in the long run as well.

Fourth, what is the probability that the Chinese government will actually use its country's economic ties with the Netherlands in ways that harm Dutch security? There is no doubt that China occasionally uses its economic influence to support foreign policy objectives that go beyond the economic domain. To an extent, this is common to all great powers, including the US and the EU. But the relatively close proximity between state and business in China enables the Chinese government to exert foreign economic pressure (or provide inducements) without using formal sanctions, and to use its economic influence to underpin a wider range of political aims than Western governments are able to do.

A very visible current instance of China informally sanctioning an EU country is the undeclared blockade of Lithuanian exports to China. The Chinese government initiated this de facto blockade in 2021 after the Lithuanian government allowed Taiwan to open a representative office in Vilnius under a name that China regards as a move away from the status quo in Sino-European relations on matters relating to Taiwan. However, in the past, the Chinese government has also leveraged China's economic influence in its diplomatic relations with the Netherlands. This happened in the 1980s and early 1990s when China initially wanted to prevent the sale of two navy submarines to Taiwan, and later to induce the Dutch government to refrain from allowing further sales. At first, the Chinese government threatened to obstruct access to the Chinese market for Dutch companies, but later promised to purchase Dutch-built ships and airplanes. Another instance of political leverage occurred in 1997 when the Chinese government postponed the incoming visit of a large Dutch political and business delegation after the Netherlands, as rotating chair of the EU, prepared a statement critical of China at the UN Commission on Human Rights. The mission was aimed at helping Dutch companies expand their presence in the Chinese market. The Chinese reaction was primarily a signal that, for foreign countries, market access in China is dependent on refraining from mobilizing international pressure on China in relation to human rights. The latter is seen by the Chinese political leadership as undermining the position of the Chinese Communist Party.

Based on the Dutch experience, it seems that China leverages its economic influence only for a limited and very specific number of foreign policy aims. These include, so far, issues related to Taiwan and human rights. Whether other issues, such as Chinese investors' access to the Netherlands or possible future Dutch naval activities in the South China Sea, are or may become relevant is unclear, but from a Dutch point of view it must be assumed that this is possible. While there has been a high degree of continuity in terms of the priorities in Chinese foreign policy in past decades, the current relationship between China and Europe is more tense and more complicated than ever before.

Apart from being a potential tool of influence, economic interaction can also be used by states to inflict damage through sabotage in case of war or to obtain intelligence. Should a war erupt between the US and China and should the Netherlands support the American side, this would probably severely disrupt Sino-Dutch economic interaction. In other words, once a situation emerges in which the Chinese government might want to use China's economic presence in the Netherlands for acts of sabotage, China's actual economic presence would probably decline very rapidly. The use of economic interaction to support intelligence gathering is not related to a situation of conflict and is something that the Chinese government might engage in at any time. However, the use of Chinese companies as intelligence-gathering tools runs the risk of this damaging not only the companies involved, but also China's foreign economic relations at large. It therefore seems likely that the Chinese government prefers ways of intelligence gathering for security-related purposes that do not involve Chinese companies that are engaged with Dutch counterparts. Direct cyberattacks against Dutch targets that are orchestrated by Chinese intelligence organizations would seem an effective and less risky approach. According to Dutch intelligence agencies, China is a major source of cyberattacks targeted at data gathering.[8]

Fifth, how would instances of Chinese use of economic influence for political purposes affect Dutch national security? Another insight gleaned from Dutch experiences between 1980 and 1997 is that the Chinese government uses economic influence not only for coercion or deterrence, but also as an inducement (e.g. offering to import ships or airplanes). Moreover, tensions with China in the 1980s and 90s over Taiwan and human rights did not have a significant impact on the Dutch economy, in either a negative or a positive way. Still, from a national security perspective, it is not inducement but coercion that is the focus of attention. Furthermore, China's economic power, the self-assuredness of its behaviour and level of ambition as a great power have increased enormously since the late 1990s.

The aspect of Dutch national security that would be affected the most is what the Dutch government calls economic security, which it has subdivided into three distinct topics: uninterrupted vital economic processes, the integrity of economically relevant information and data flows, and avoidance of strategic economic dependencies.[9] While the first two topics are straightforward, the third is more complicated. It entails the emergence of long-term dependencies that cannot be abandoned without incurring severe economic damage other than disrupting vital economic processes or damaging the integrity of data flows. An example of this is one or more Dutch 'non-vital' sectors, such as semiconductor firms, shipbuilders or car industry suppliers, being dependent on Chinese standards or raw materials. By using economic influence as a strategic instrument, the Chinese government can potentially harm Dutch economic security in all three areas of economic security.

8 See https://www.rtlnieuws.nl/tech/artikel/5214049/cyberdreiging-uit-china-en-rusland-groeit-veiligheids-diensten-slaan-alarm.
9 See https://www.nctv.nl/onderwerpen/economische-veiligheid.

Dutch policies since 2013

In responding to the potential harmful effects of China's economic influence, the Dutch government has focused in particular on foreign direct investment and the use of Chinese technology. Formally, Dutch policies related to hybrid threats and economic security are 'country neutral': they are not aimed at any specific state actor. However, in practice, concerns about China's influence have been among the drivers behind the development of such policies.

The first phase of heightened Dutch concern about Chinese economic influence occurred between 2013 and 2017 and was mainly related to investments. At this time there was a surge in Chinese direct investment in the Netherlands,[10] among other EU countries. Russian interference in the civil war in eastern Ukraine and the illegal Russian annexation of Crimea also alerted European governments to the relevance of hybrid threats and of geopolitics for mainstream international relations. The so-called US pivot to Asia signalled to Europe that, despite the crisis in Ukraine, the US was increasingly focused on China.

The immediate trigger for policy adjustment in the Netherlands was the 2013 attempt by a Mexican company (América Móvil) to purchase the main Dutch telecom provider (KPN). Although the take-over bid did not succeed, it pointed to the possibility that a foreign state-owned company, for instance from China, might acquire an influential position in the Dutch telecom sector. **The Dutch government duly decided to upgrade its tools for screening and potentially blocking certain foreign take-overs in the telecoms sector.**

At the time, the Netherlands did not have a generic investment screening system. **The government's position in this regard appeared to be that the state should interfere in market processes as little as possible, and that it was sufficient to have sector-specific tools for oversight (for instance for energy and banking).**[11] Part of the background to this may have been that the Netherlands had long been home to large multinational enterprises such as Royal Dutch Shell, Unilever and Philips, and had therefore benefited from free flows of direct investment between countries. Moreover, the Netherlands had a successful approach to attracting foreign investors, supported by favourable tax rules. By late 2017, when the European Commission was preparing an EU-wide framework for national screening of foreign direct investment, the Netherlands government was still sceptical about the desirability of generic screening.[12] The European Commission initiative came after Germany, Italy and France had promoted the idea of a common EU approach to investment screening. This move, in turn, appears to have been prompted in part by the take-over of a German robotics firm (Kuka) by a Chinese company (Midea) in 2016.

In the second phase, which started in 2018 and is still ongoing, the Dutch government adopted a different attitude towards generic investment screening. Sometime during 2018 the government switched to a supportive

10 See https://www.clingendael.org/sites/default/files/2020-12/Policy_brief_China_geopolitics_investment_Netherlands_December_2020_0.pdf.
11 These notions were integral to the objections raised by the Dutch government in December 2017 against the European Commission's proposal to introduce an EU-wide investment screening framework: https://zoek.officielebekendmakingen.nl/kst-22112-2437.html.
12 See https://zoek.officielebekendmakingen.nl/kst-22112-2437.html.

stance on the screening framework, as proposed by the European Commission.[13] The shift in the government's attitude apparently reflected the overall change in European views on China, which became more negative around this time.[14] This shift coincided with, and may have been stimulated by, a conspicuous increase in anti-China rhetoric from the US government under President Donald Trump, more repressive Chinese policies in the Xinjiang autonomous region, and deteriorating China-Taiwan relations. In addition, non-China-related developments such as growing doubts about the US as a reliable partner and the UK's exit from the EU may have contributed to a recalibration of the Dutch stance on investment screening (and on the need to align foreign policy with that of Germany and France).

In April–May 2022, in line with the EU screening framework that had been operational since 2020, the Dutch parliament adopted the Investment Screening Act of the Netherlands that had been prepared by the government.[15] Consequently, the Dutch government established an investment review agency under the ministry of economic affairs.[16] **For the first time, the Netherlands now has a generic mechanism for investment screening.** The main focus of the mechanism is on security implications in relation to vital economic processes (energy, banking and transport hubs) and sensitive technology. The latter refers to technology that plays a role in military and dual-use activities, intelligence, and national security.

A number of assessment criteria for screening on sensitive technologies are particularly relevant in the case of Chinese investments: the lack of separation between civilian and military research and development, acquisition that is not driven exclusively by commercial aims, the investor's home government having an offensive programme to acquire a technological or strategic position of power, and the likelihood of the investor limiting access to a sensitive technology post-acquisition for non-commercial motives.

The emphasis on sensitive technology reflects a broader development in the second phase of Dutch policies to respond to Chinese economic influence. This also relates to concerns about the use of Chinese technology in ways that are not necessarily connected to direct investments. An important development in the government's stance on sensitive technologies since 2018 has been its response to possible Chinese involvement in the new 5G telecommunication network. Like various other European and Western countries, the Netherlands hesitated over whether it would ban Chinese equipment from the new 5G network. Pressure from the US as well as concerns about possible sabotage, data theft, and strategic dependency may have contributed to Dutch wariness of Chinese equipment. At the same time, the Dutch government's standard approach of avoiding policies aimed at any particular country was complicated by the fact that the only non-EU companies capable of

13 European Commission, 'Proposal for a Regulation of the European Parliament and of the Council establishing a framework for screening of foreign direct investments into the European Union', 13 September, 2017, https://eur-lex.europa.eu/resource.html?uri=cellar:cf655d2a-9858–11e7-b92d-01aa75ed71a1.0001.02/DOC_1&format=PDF.
14 See https://www.pewresearch.org/global/2020/10/06/unfavorable-views-of-china-reach-historic-highs-in-many-countries/.
15 See https://zoek.officielebekendmakingen.nl/stb-2022–215.html.
16 See https://www.bureautoetsinginvesteringen.nl/.

supplying 5G technology for public networks were Huawei and ZTE of China. The government did not ban Chinese equipment completely but made sure that it could not be part of the core 5G network. In 2021 the main Dutch telecom providers were reported to still be buying Chinese technology for non-core functions.[17] In general, the Dutch approach to using Chinese equipment seems ad hoc rather than standardised. For instance, in 2021 the Dutch media reported that the Dutch police and some other government agencies were using China-made drones (produced by DJI), while the Dutch military refrained from using them due to security concerns.[18]

Even though Dutch policies aimed at protecting economic security are not country-specific, **the Dutch government is explicit in naming China as a potential threat to economic security.**[19] It seems clear therefore that the above-mentioned policies are designed at least in part to address concerns that relate to Chinese economic influence. The government is currently preparing a policy framework for whole-of-government responses to (particularly hybrid) threats from state actors.[20] However, this policy framework is not yet operational and no information is as yet publicly available. Finally, it should also be noted that **Dutch policies to deal with security implications of foreign economic influence are closely linked to efforts at the EU and NATO levels.**[21] Apart from investment screening, another approach for which the EU level is important is diversification of supply chains in order to be less dependent on China. One of the reasons why the Dutch government is supportive of the European Commission's proposal for a European Chips Act is that it would help avoid the EU becoming dependent on chip supplies from foreign states such as China. Tensions with Russia over its invasion of Ukraine and the related energy crisis have further spurred the Netherlands to work with the EU to decrease strategic dependencies.

17 See https://www.rtlnieuws.nl/tech/artikel/5232314/huawei-5g-telecom-netwerk-provider-kpn-t-mobile-vodafone-china-spionage.
18 See https://www.platform-investico.nl/artikel/politie-gebruikt-omstreden-chinese-drones-voor-opsporing/.
19 NCTV, 'Midterm Review 2021: Nationale Veiligheid Strategie', 2021, 9–10.
20 NCTV, 'Midterm Review 2021', 10.
21 See https://www.rijksoverheid.nl/documenten/kamerstukken/2022/11/08/kamerbrief-inzake-open-strategische-autonomie.

Conclusions

For the Netherlands, the main current vulnerability stemming from economic interaction with China is that it can lead to strategic dependencies. The Chinese government could potentially take advantage of such dependencies to pressure the Dutch government into doing or not doing certain things in relation to issues that it regards as high priority matters. The economic importance of China for the Netherlands is primarily related to the benefits that the Dutch economy derives from trade between China and Germany, which appear to be substantial. Additional benefits relate to market access in China, and access to Chinese capital, products, technology and talent.

On the other hand, there are limits to China's leverage due to its own dependencies on the Netherlands and the EU as a whole. Other national security vulnerabilities that may come with economic interaction, such as potential sabotage of vital processes or security-related information theft, also appear limited. Nonetheless, this does not mean that the Dutch government can afford to leave them unaddressed. From a Dutch national security point of view, having the ability to act largely independently of Chinese influence in matters where Dutch and Chinese interests conflict, anticipating and preparing for a possible conflict between the US and China, and minimising potential damage to national security that results from espionage by the Chinese state via Chinese companies are relevant aims.

The new Investment Screening Act (which is expected to become active around the end of 2022 and which will apply retroactively from 8 September 2020) is the most visible outcome of Dutch government action to limit vulnerabilities related to economic security. Other efforts are less visible, such as diversifying supply chains, coordinating within the EU or the response to potential Chinese involvement in 5G, or have not yet been made public, such as the new policy framework for responding to state actor threats. Still, it seems that from 2018 the Dutch government has been very active in dealing with potential negative effects of economic interaction with China. While the investment screening mechanism applies only to investments made after the surge that occurred up to 2018, it is nonetheless important since it provides the government not only with a screening agency, but also with a set of criteria to assess the security implications of foreign influence – especially in relation to sensitive technologies – that may also be relevant in areas other than direct investment.

Based on the information that is publicly available, the ongoing efforts of the government to increase Dutch economic resilience (and to do so together with the rest of the EU) seem to coincide, by and large, with the increased awareness that economic relations with China can have national security implications, and the EU's increasingly tense and complex relationship with China. The key issue that currently remains to be addressed by the Netherlands is how to develop a clear idea of China's economic importance. The degree to which vulnerabilities that stem from exposure to Chinese economic influence are acceptable depends on the potential damage involved and on the possible gains that the cooperation with China can bring for Dutch economic competitiveness.

Economic resilience requires defensive security mechanisms as well as a strong economy. Under the current circumstances, a precise assessment is needed of the relationship between the risks and benefits of Dutch economic relations with China.

Author

Dr Frans-Paul van der Putten is a Netherlands-based independent researcher and consultant on China and geopolitics. He has non-employee affiliations with the Clingendael Institute (as a Senior Research Associate) and Leiden Asia Centre (as a Researcher). He is a former Senior Research Fellow at the Clingendael Institute (2007–2022), where he co-founded and acted as the coordinator of the China Centre (2019–2022) and as coordinating editor of Silk Road Headlines (2015–2022). He can be reached at fputten@chinageopolitics.nl.

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