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The EU's approach to tariffs on Chinese electric vehicles

Provisional European Union tariffs on Chinese electric vehicles are scheduled to enter into full effect for a period of up to five years on 31 October 2024. This followed the imposition of more stringent measures by the United States and Canada.

Whereas the US and Canada have raised tariffs on Chinese EVs to 100% across the board and included tariff hikes on other materials and intermediate inputs in the EV supply chain, the EU tariffs are levied according to company and cover EVs only.

On 4 October 2024, the European Commission voted to enact the provisional tariffs on Chinese imports of electric vehicles (EVs) that had been in place since early July, when the commission released the findings from its nine-month investigation into subsidies and overcapacity in China's EV industry. Typically, investigations into anti-subsidy or countervailing duties are conducted at the request of private sector firms; in this case, however, the commission initiated the study on an ex officio basis (that is, without such a request having been made). Ten member states, including France and Italy, voted in favour of implementing the legislation, while Germany and Hungary were among the five opposing the measure. There were 12 abstentions. The tariffs are set to take effect on 31 October 2024 and are scheduled to remain in place for five years.

The European Union's actions follow separate measures implemented by the United States and Canada in late September and early October, but take a different approach. Whereas the US and Canada have raised tariffs on Chinese EVs to 100% across the board and included tariff hikes on other materials and intermediate inputs in the EV supply chain, the EU tariffs are levied according to company and cover EVs only. For example, EVs produced by China's Shanghai Automotive Industry Corporation will face the highest rate, 35.3%, and those made by the firms Geely and BYD face tariffs of 18.8% and 17%, respectively. These are in addition to the 10% tariff the EU already imposes on all car imports. European and US manufacturers of EVs such as Tesla will face lower rates on their exports from China to the EU, but will still see them rise.

The rationale for EU policy action

The EU faces a different trade- and investment-policy environment with China than the US and Canada, especially regarding EVs. Chinese EV exports to the EU have surged over the last three years, rising from 33,371 vehicles in 2020 to 485,500 during the EU's investigation from October 2022 to September 2023. Canada, for its part, also saw a year-on-year jump of 460% in EV imports from China in 2023, with the number of vehicles – mainly from Tesla's Shanghai plant – rolled off at the Port of Vancouver exceeding 44,000. In the US, however, Chinese EV imports constitute only 1–2% of a relatively small market.

Meanwhile, European car manufacturers both export to China from the EU and have joint ventures with Chinese companies to produce for China's domestic market and export. Chinese manufacturers of EVs and batteries are also investing heavily in their European supply chains. As of October 2024, there are three Chinese battery plants in Germany, an EV plant in Poland, two EV plants and two battery plants in Hungary and an EV plant in Spain. More investments are planned.

By comparison, Chinese investment in EV and battery production in the US has so far been limited. BYD produces electric buses in California; Volvo, which is owned by Geely, has an EV plant in South Carolina. Gotion, the US subsidiary of a Chinese firm, is constructing EV-battery factories in Illinois and Michigan. But there appears to be little else in the pipeline. No Chinese EV or battery firms currently have factories in Canada, although BYD is reportedly considering an investment. Even though that may not come to pass, the government of Justin Trudeau has published options for blocking Chinese EV firms from its market, including restricting investment.

More than overcapacity and subsidies

The aim of the European Commission's study into China's EV industry was narrow. It was only to determine whether EV production in China was – and is – being subsidised to the extent that it violates the rules of the World Trade Organization, which would justify the EU implementing countervailing duties. That is what the study found, and that is what the EU has voted to do. In addition, the study concluded that 'China already has an overcapacity for [EVs] that will largely be used for export to [the EU] market'.

Overcapacity – or excess supply – was also cited by the Department of Finance Canada as one of the reasons for tariffs on Chinese EVs when it announced a request for consultations in July, labelling overcapacity a 'state-directed, intentional' policy on the part of China. The finance ministry went beyond that, however, to note concerns about environmental and labour standards and the need to prevent 'trade diversion' as a result of 'recent actions' taken by its trading partners. Although the European Commission's report was not explicit on the point, trade diversion is also a concern for the EU. With the US effectively banning EV imports from China, China's overcapacity must be exported somewhere. Canada is not as large a market as the US or the EU, as measured by the size of its population, but its consumers are wealthy, making it a viable outlet for some of that excess supply.

A public notice published by the US Trade Representative on 18 September 2024 goes further than the European Commission or Canada:

> As a result of China's efforts to dominate the electric vehicles market, China now produces 70 percent of the world's electric cars – jeopardizing productive investments elsewhere. The U.S. Trade Representative has determined that modification to increase the duties on electric vehicles will encourage diversification from Chinese sources, while also advancing U.S. policy to incentivize the development of, and investments in, a robust electric vehicle market, reducing exposure to China's technology transfer-related acts, policies, and practices, and providing additional leverage with China to eliminate the investigated acts, policies, and practices.

There are at least two key US policies referenced here. The first is decoupling. The text labels it 'diversification', but since the administration of Donald Trump it has been clear that, to the greatest extent possible, the US is intent on reducing its reliance on China for the loosely defined range of goods it deems strategic. The second policy referenced is the Inflation Reduction Act. The tax breaks and other incentives offered by the law could benefit Chinese firms, from manufacturers of solar panels to EVs and in between. A surge in Chinese-made EVs in the American market could therefore constrain an already struggling domestic EV-manufacturing ecosystem.

Europe cautious, the US and Canada unimpeded

As the 4 October vote showed, there is not a consensus among EU members about conducting trade and economic relations with China. That the tariff legislation passed with only ten members in support, five against and 11 abstentions suggests a policy that could prove temporary.

Among the five opposing countries, Germany, with its massive automotive sector, has a clear interest in maintaining access to China's market, mainly for combustion-engine vehicles. Hungary, which also voted against the tariffs, is home to four Chinese investments related to EVs and EV batteries. Its leader, Viktor Orbán, visited Beijing last summer and has warned of an 'economic cold war' with China. China is pursuing a strategy of targeted retaliation against those members that voted in support of the tariffs. This is similar to its actions following the US imposition of tariffs during the Trump administration, when China raised tariffs on US bourbon, motorcycles and agricultural products. In the case of the EU, it has threatened to impose tariffs on French cognac, Spanish pork and dairy from various countries.

Given that the number of countries abstaining or voting 'No' exceeds the number supporting tariffs, there is some chance that the policy will not remain in place for a full five years. Already, the European Commission and China are attempting to negotiate a settlement. The commission, however, rejected China's immediate offer to set a minimum price for its EVs in the EU market at €30,000 (US$32,393). This is to be the final offer.

At the same time, China is also attempting to retaliate against Canada by initiating an anti-dumping investigation into Canadian canola exports. Canada is the world's largest exporter of canola, also known as rapeseed, and China's largest supplier. There are few alternatives for China to meet domestic demand. It has banned canola imports from Australia due to the blackleg fungus, which infects oilseeds, and supplies from Europe and Ukraine are tight. Russia could replace some of the shortfall, but not all, if Canadian imports were stopped. This undercuts the credibility of the Chinese threat.

So far, China has not threatened retaliation against the US. One US Treasury official claimed that, after a bilateral meeting in Beijing in early October, Chinese economic officials gained a 'more nuanced understanding' of what the US was trying to accomplish with the tariffs, namely its approach to industrial policy. Once a new president is inaugurated in 2025, Beijing may well attempt to target farmers in soybean-producing states, as it did during the Trump administration.

Outlook

Of the EU, the US and Canada, the EU is the only one that would consider backtracking on its EV tariffs. Spain, for one, changed its vote from 'Yes' to abstention after Prime Minister Pedro Sánchez met with President Xi Jinping in September. Should Beijing proceed with threatened pork tariffs, it might be enough to move Spain into the opposition. Short of that, there remains room for a negotiated compromise between Brussels and Beijing, although it will prove complex, not least on the enforcement side. Holding Beijing to commitments is difficult, as the US discovered when China did not deliver on its agreement to import an additional US$200 billion in US goods and services. That is a lesson surely not lost on policymakers in major European capitals.

It is hard to envision either the US or Canada rescinding their tariffs. There certainly will be no significant political pressure to do so on either side of the border. The administration of Joe Biden largely left his predecessor's tariffs on Chinese goods in place. The recent increases – on not only EVs and batteries but also semiconductors, personal protective equipment and other goods deemed strategic – represent an escalation. Vice President Kamala Harris is unlikely to break with the current administration's policy if she wins the presidency. Trump has pledged to increase tariffs on all Chinese imports to at least 60% and raise EV tariffs to 200% or above if he wins. The latter move would be largely symbolic, since any rate above the current 100% would not be significantly more prohibitive.

One scenario that is easier to envision is greater trade tension between the EU and the US due to China shifting more exports – not just EVs – that might have otherwise been bound for the US eastward to Europe. In addition, if Trump wins a second term in November, he will likely increase tariffs on all countries, with transatlantic trade and economic cooperation eroding further as a result.

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