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CHINA'S DIRECT INVESTMENT IN THE EUROPEAN UNION: CHALLENGES AND POLICY RESPONSES

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China's Direct Investment in the European Union: Challenges and Policy Responses

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ABSTRACT:

The dramatic rise of Chinese direct investment into the European Union has sparked a debate about the control that China may be seeking to take over European economies. Quite naturally these concerns have led to repeated calls that action be taken to slow down, if not to halt entirely, this growing trend. The objective of the paper is to shed light on this debate. Following a thorough analysis of Chinese direct investment in the EU, the paper suggests that the challenges posed by these inflows are widely overblown. Despite this, the paper concludes that it is necessary to have a systematic approach to regulating inbound foreign investment (including from China) in the EU. Such an approach may help guard against the risk of a protectionist drift inside the EU, as well as the possibility that some investors may one day pose a threat to national security. The paper concludes that although the current fragmented regulatory approach is unsatisfactory, due to the difficulties associated with a unified EU-wide review process, the most realistic option is to promote a more systematic and coordinated use of existing mechanisms such as competition policy. Also, pushing for the negotiation of a China-EU BIT is certainly a promising avenue to enhance the EU's bargaining leverage based on the principle of positive reciprocity.

Keywords: China, EU, foreign direct investment, national security, protectionism.

JEL classification: F13, F21, F23, F50.

China's Direct Investment in the European Union: Challenges and Policy Responses

Françoise Nicolas

1. Introduction

The rise of Chinese direct investment into the European Union (EU) has attracted a lot of (often negative) public and media attention over the past few years. In France, for instance, Chinese investments in many diverse local companies, including wineries, have sparked a debate about the control that China may be seeking over the French economy. Although these allegations are clearly ill-founded, the emergence of investments by state-backed Chinese entities has raised concerns, particularly at a time of crisis when some European companies are under financial duress and risk being sold at well below their actual value. A striking example is the acquisition in 2009 by state-controlled China Ocean Shipping Company (COSCO) of part of the container port of Piraeus (Pier II) for 35 years, as well as its investment in a third pier to enhance the port's capacity. Quite naturally, many who fear that all national assets will end up in the control of a foreign power are demanding that action be taken to slow down, if not halt entirely, the growing trend of rising Chinese investment in the EU.

The objectives of the paper are to shed light on rhetoric against Chinese investment in the EU, to assess the magnitude of the alleged threat posed by Chinese direct investment, and to suggest ways of dealing with it. The first section provides an overview of Chinese direct investment in the EU. The second section examines the motivations of Chinese investors and the impact of their investments on European economies in order to assess the extent to which they constitute a threat. The third section analyzes the current policy responses at the national and European levels and suggests how the EU could move forward on this issue.

2. Chinese Direct Investment in the EU: Trends and Patterns¹

2.1. How Much? Still Modest but Growing Rapidly

Chinese direct investments in the EU are growing rapidly by almost any absolute measure. According to data from China's Ministry of Commerce (MOFCOM various),² they grew from about US\$150 million per year from 2004 to 2006 to roughly US\$1 billion in 2007; after a sharp decline in 2008, they reached US\$3 billion in 2009, US\$6 billion in 2010 and US\$7.6 billion in 2011.³ By 2011, there were more than 1600 subsidiaries launched by Chinese enterprises in the EU, with 50,000 foreign employees (MOFCOM various).

Despite this dramatic rise, the EU emerged as a target for Chinese firms only after 2003, and Chinese ODI into the EU remains modest in relative terms, accounting for a very small share (less than 2%) of total FDI inflows into the EU (Eurostat Database). In terms of stock, China owns only 0.40% of the €3807 trillion of foreign FDI in the EU in 2011 (Eurostat Database).

The EU may not be the number one destination for Chinese ODI in terms of stock, but in terms of growth rates it has outpaced other regions such as the United States in attracting

¹ This section focuses primarily on recent features of Chinese FDI inflows into Europe. For an earlier assessment see, for instance, Nicolas (2009) or Nicolas and Thomsen (2008).

² All bibliographic references to MOFCOM in this paper are to the *Statistical Bulletin of China's Outward Foreign Direct Investment*, various issues; <http://english.mofcom.gov.cn/article/statistic/foreigninvestment>.

³ In the wake of the global financial crisis, China's ODI flows held up better than those from industrialized countries, with an annual rise of 46% on average between 2007 and 2010. In 2012, for the first time ever China became the third largest investor in the world after the United States and Japan (it still ranked sixth in the world in 2011).

ODI from China in recent years.⁴ Similarly, from a European perspective, Chinese investments are the most rapidly growing inward flows. In Germany for instance, Chinese ODI multiplied by 20 between 2003 and 2011 (Jungbluth 2013, 14). It is important to emphasize that so far as perceptions are concerned, the trend of rapidly rising Chinese investment in the EU matters more than the absolute amount being invested.

2.2. How? The Rise of Mergers and Acquisitions

At the global level, in numerical terms Chinese greenfield investment projects outpace cross-border mergers and acquisitions (M&As). However, the former tend to be quite small in value (and include the establishment of a large number of trade representative offices) while the role of M&As by Chinese enterprises has been on the rise during recent years. M&As accounted for 43% of China's outward FDI in 2010 compared to just 18% in 2003 (Xu, Petersen, and Wang 2012, 8).

The same observation holds true for Chinese ODI into the EU: while the number of greenfield investments is substantially larger than the number of M&As, the value of the latter is much higher than that of the former (Hanemann and Rosen 2012, 34).⁵

Who are the Targets of M&As?

The figures from recent years show a significant rise in mainland Chinese M&A activity in the EU, in both volume and value terms (PWC 2012, 10), and a narrowing of the gap in deal flow between the two types of transactions.

⁴ The sharp rise observed over the past few years should, however, be qualified as it is largely due to substantial flows to Luxemburg which has a favorable tax regime but is not the final destination of these flows.

⁵ Interestingly, China's Europe-bound deals are now dominated by mainland China and no longer by Hong Kong firms.

The very high value transactions by China in the EU that attracted the most media attention have been in the Energy, Utilities and Financial Services sectors.⁶ But a deeper look at the data suggests that: (1) a large proportion of Chinese deals fall under the €100 million mark; and (2) the industrial products sector is the one that sees the most Chinese M&A activity. This should not come as a surprise since China is the world's largest manufacturing nation.

In the EU, one can identify three main categories of firms targeted by Chinese acquirers in the industrial products sector. The first category refers to ailing or financially distressed firms, such as Shenyang's acquisition of Schiess or Chongqing Light and Textile Group's acquisition of Saargummi.⁷ The second category includes competitive niche producers, with China Bluestar acquiring Rhodia Silicones for instance. And the third category is made up of former partners or sub-contractors/suppliers, as in the case of Chalkis and Le Cabanon-Conserves de Provence. These investments sometimes take the form of outright acquisitions or start with a strategic investment which is eventually followed by a complete takeover. Chinese firms also sometimes engage in minority stake acquisitions simply as a way of strengthening the relationship with their European partners. These strategic investments occur both in services (with China Development Bank and Barclays, or

⁶ By way of illustration, 75% of the total amount of Chinese ODI into the EU27 in the first quarter of 2012 is explained by the US\$1.0 billion acquisition of Kalahari Minerals PLC in the UK by China Guangdong Nuclear Power (TAC 2012).

⁷ If the German case is any guide, however, it seems that Chinese investors are gradually shifting away from the acquisition of ailing companies (Jungbluth 2013, 13).

Ping An and Fortis for instance) and in manufacturing (for instance, Ningbo Bird, a leading Chinese mobile phone producer, chose to engage in equity partnership with France's Sagem).

(Table 1 about here)

Greenfield Investments

Many greenfield investments aim to support existing corporate activities through the establishment of trade representative offices as well as through investments in logistics. However, the presence of Chinese firms in maritime transport and logistics services is also indicative of their desire to retain control over the logistical chain. Moreover, Chinese investors also seek to develop 'commercial hubs', with the objective of helping small and medium sized Chinese investors gain access to the European market. Such hubs are envisaged in Finland, Italy, Hungary, Poland, the Netherlands and the Czech Republic (Hay et al. 2008, 62).

Greenfield investments are also common in the telecommunications industry as well as in other services. For example, CCTV opened its new European headquarters in London, COSCO Logistics has established a subsidiary in the United Kingdom (UK) and two subsidiaries in France, and China Shipping followed a similar strategy. In another case, China's Bank of Communications opened a new branch office in Frankfurt, its first branch office in Europe.

Lastly, greenfield investments are common for the establishment of R&D centers. Some of these centers are used to adapt Chinese products to the local market,⁸ but the location of these centers is also clearly indicative of their aim to capture the externalities created by host-country technology clusters.

⁸ Huawei has R&D centers in France, Sweden, Germany, the Netherlands and Spain, aimed at customizing goods and services for the local market.

2.3. *Where? France, Germany and the UK as the Top Three Destinations*

With the exception of MOFCOM data,⁹ all sources rank France, Germany and the UK as the top three destinations for Chinese ODI in the EU (Hanemann and Rosen 2012, 38; Milelli 2012, 65). Behind the top three destinations, Spain and Italy are also significant recipients of Chinese ODI, together with several New Member States¹⁰ such as Poland and Romania.

However, which one of the top three destinations ranks first varies across data sources and means of measurement. Official Chinese statistics showed Germany consistently ahead of the UK, but France was ranked first in 2011 (MOFCOM various). By contrast, private sources used to suggest that the UK is a major magnet for Chinese ODI. In 2008, 350 Chinese firms were already present in the UK and London was attracting 15% of the Chinese investment capital flowing into Europe at the time (Ernst and Young Investment Monitor 2008). But the balance has been shifting in Germany's favor. According to PWC (2012), Germany now overtakes the UK as a destination for mainland China M&As. According to other sources, in terms of the number of deals, Germany ranks as the number one destination for Chinese investors ahead of (in order of importance) the UK, France, the Netherlands, Italy, and Spain (TAC 2012). In 2011, for instance, Germany is said to have secured twice as many Chinese projects as the UK (Ernst and Young 2012).

(Table 2 about here)

2.4. *Who? The Rise of Private Firms and Sovereign Wealth Funds*

Traditionally, China's State-Owned Enterprises (SOEs) have been the main driver of Chinese

⁹ According to MOFCOM data, Luxemburg is the largest destination for Chinese ODI in Europe. But it is notoriously known as a mere gateway and not the final destination of FDI flows.

¹⁰ The 'New Member States' refers to the 10 states that became members of the EU in May 2004.

ODI, accounting for more than two thirds of total Chinese ODI worldwide (MOFCOM various). The capacity of private Chinese companies for outward FDI is relatively low due to their limited access to funding, technology, and market influence.

As is the case in the rest of the world, in Europe the vast majority (90%) of the very high value deals by Chinese investors involved SOEs or Sovereign Wealth Funds (SWFs).¹¹ The latter have been particularly active over the past few years, in line with China's effort to simultaneously diversify the use of its foreign exchange reserve and ensure access to resources. Of the 20 biggest Europe-bound M&A transactions from mainland China, five were made by Chinese SWFs.¹² By way of illustration, the China Investment Corporation (CIC) acquired:

- a 30% stake in French GDF Suez's gas exploration and production division in December 2011;
- an 8.7% stake in UK utility group, Thames Water, the following month; and
- 2.3% of Apax Partners LLP, a private equity partnership in February 2010.

Similarly, in April 2008 the State Administration of Foreign Exchange (SAFE) took a 1.6% stake in Total's capital and a 1% stake in British Petroleum (BP). After SOEs and SWFs, private firms like Geely or the Sany Group also account for a substantial number of deals even if they are not necessarily large in value terms.

2.5. Which Activities? Highly Diversified Investments

As shown in Table 1, Chinese investors are present in a wide range of sectors. As recalled

¹¹ This refers to the period 2006 to 2012 (PWC 2012).

¹² In China, two institutions may be considered SWFs: the China Investment Corporation (CIC) and the State Administration of Foreign Exchange (SAFE) through the SAFE Investment Company.

earlier, large deals are primarily in the Energy, Utilities, Mining and Infrastructure (EUMI) sectors. The strategic significance of these sectors accounts for the intense media coverage of these deals. The US\$3.5 billion strategic partnership between the Chinese Three Gorges Corporation and electric utility company, Energia de Portugal, is a case in point.

Although large EUMI deals are the most valuable, other sectors are actually seeing a rising number of EU-bound M&A transactions.¹³ The industrial products sector accounted for about 30% of all transactions over the period 2006-2012 (PWC 2012, 12).

Investment in R&D is still marginal but is rapidly rising. In Europe, Chinese firms accounted for a mere average of 1.7% of the R&D projects by foreign investors over the period 2001 to 2005, rising from virtually zero in 2001 to reach 2.8% in 2006 (Hatem 2006, 14). The same holds true for other activities, in particular headquarters and shared services centers. From zero in 2002, the share of Chinese projects in these activities rose to 4.7% in 2005 (Hatem 2006, 21).

To some extent, Chinese ODI does not target the same sectors in the various European countries. For instance, the UK tends to attract more headquarters than France or Germany. In France, Chinese firms are present in a wide variety of sectors, spanning chemicals, textiles, electronics and telecommunications equipment, consumer electronics, air transport and freight, electrical home appliances, as well as energy and utilities. The major Chinese firms present in France are Zhong Xing Telecommunication Equipment (ZTE), Huawei, COSCO, Watchdata and BlueStar (a subsidiary of ChemChina).

Chinese M&As in Germany are primarily concentrated in the electronics and machinery industries (machine-tools as well as automobile sub-contractors). Also, while they used to involve the acquisition of financially troubled local firms, this is no longer the case (or

¹³ The particular sectors that are experiencing rising M&As are the industrial products sector – from automotive to chemicals – followed by Telecommunications and Media, and Business Services.

at least is not as frequent). Until 2010, a substantial number of acquisitions targeted insolvent firms filing for bankruptcy,¹⁴ but from 2011 onwards financially sound firms were also targeted.¹⁵

In the UK, major acquisitions have been undertaken in the automotive sector. As early as 1997, Wanxiang bought a 60% share of the AS Company (UK), which sells bearings in the European market, and established Wanxiang Europe Bearing Company as a beachhead in Europe. In 2005, Nanjing Auto acquired some assets of British MG Rover's car making operations. Similarly Huaxiang, one of China's largest car-parts manufacturers, took over British Lawrence Automotive Interiors, a world class manufacturer of premium decorative trim components for luxury cars. In terms of value, however, investments in the Energy, Utilities and Mineral Industries are substantial, squaring with the desire of Chinese investors to access natural resources. Chinese investors are also present in the financial sector: China Development Bank (CDB) teamed up with Singapore's state-owned investment vehicle, Temasek, to successfully acquire a 3.1% stake in Barclays in July 2007 for over US\$3 billion.

In the New Member States, Chinese firms are primarily active in the consumer electronics and white goods industries, as well as in the automotive industry. In an ironic twist, Hisense established its factory in Hungary in a building that had been vacated by Microsoft when it moved its production to China (Accenture 2007, 10). In these countries, Chinese investments tend to be production-oriented and primarily efficiency-seeking. Such is the case with the Hisense, Changhong, Skyworth, Haier and TCL groups, which have established overseas production bases and joint ventures in countries such as Hungary, the

¹⁴ These acquisitions were of German companies such as Schneider Electronics AG, Welz Gas Cylinder, Lutz Maschinen, Schiess, Waldrich Coburg, Kelch and Assyst Bulmer.

¹⁵ See, for example, Chinese acquisitions of Rohde und Schwarz, Emag salach, KSM Castings, Medion, Tailored Blanks, Kiekert, Putzmeister, Schwing, Kion, Aweco, and Pfaff. For more details see Jungbluth (2013).

Czech Republic, Poland, and more recently Romania, with the aim of catering to the rest of the EU market. It remains to be seen how long such a strategy will last because of the growing need to customize production for local markets in the older EU member countries. Some signs already suggest that Chinese firms have begun to change strategies and move production to Western Europe (Hay et al. 2008, 108).

3. Assessing the Motivations and Impacts of Chinese Investments

3.1. The Public Perception of Chinese ODI: Contrasting Views across the EU

As explained above, over the last few years, Chinese investments in the EU and in particular in France, Germany and the UK have risen to unprecedented heights. This has led to worries that China may be taking control of European economies. The terms of the debate are, however, different between France, Germany and the UK, for each of these three economies has a different exposure to international trade flows.

There are many voices in France, both on the far left and the far right, who are calling for the establishment of stringent regulations in respect of Chinese investments.¹⁶ The argument often made in favor of establishing these rules is the protection of local workers, wages, and industries. For many, it is not possible and will never be possible for French workers to compete in cost terms with Chinese workers. It is therefore often suggested that French workers and companies should concentrate on high-end products. But if French firms choose to adopt this strategy, there is a view that Chinese investments would be a straightforward means for China and its enterprises to gain the elaborate knowledge they lack, force technology-transfers, and let go of the French companies when they have lost their use.

¹⁶ French sovereignist politician Nicolas Dupont-Aignan predicted that ‘we're going to put ourselves in the wolf's mouth, once we've taken this money that I call dirty money...it is like "prostituting" Europe’ (quoted in Meunier 2012, 6).

Germany, on the other hand, does not have the same qualms as France does with regard to Chinese investments. The first reason is that the situation of the economy beyond the Rhine is much better than in other parts of the EU. For German companies, China is a major trading partner with whom the quality of business is good enough to deter such worries. The absence of a chronic trade deficit with China also explains the difference. Secondly, although they have taken control of different German enterprises, the Chinese are neither equipped nor willing to really seize the German Mittelstand. Most of the small and medium enterprises (SMEs) that permeate the German economic fabric are family owned and not quoted on the stock markets. They also have a level of expertise that would be immediately lost if they were to pass to a foreign owner unable to run them in the same efficient manner.

The UK's economic history and situation is different again, which leads the country to have a different approach towards Chinese investment. Since most of Britain's industry was first privatized under Margaret Thatcher and then sold to foreign investors by her successors, the British government and public opinion are markedly less worried by Chinese investments than their continental counterparts. In spite of the efforts at rebalancing the economy that have begun under the aegis of David Cameron and George Osborne, the biggest sector in the British economy remains the financial sector. Industrial leaders like Jaguar, Rolls Royce, British Petroleum, British Aerospace (BAE) and GlaxoSmithKline have either been foreign owned for years, or have become multinational companies that no longer conduct their entire activities in the UK, thus rendering them harder to acquire by Chinese investors. It is therefore possible to say that Britain is the most relaxed of the EU members when it comes to China's growing investment frenzy.

3.2. The Reality: Chinese Investors are No Different

Chinese ODI is unusual in many respects. In spite of its size and growth, China remains a

relatively poor country, and as such would not ordinarily be expected to generate much outward investment. Furthermore, when firms from all over the world are rushing to produce in China, it is not immediately obvious why Chinese firms should invest in the opposite direction. This is especially the case given that Chinese firms do not seem to possess many of the usual competitive attributes (or firm-specific assets) that would allow them to compete directly with local firms in foreign markets. Chinese ODI is also unusual by virtue of the fact that it is dominated by state-owned firms, as outlined earlier. Despite these differences, when one looks at the motives for Chinese ODI – including by SOEs – what is surprising is how similar they are to other countries'. Like their counterparts in other countries, Chinese firms are investing abroad primarily to expand their market share in host economies. This is confirmed by a number of surveys of Chinese investor behavior as well as various econometric tests of Chinese investment patterns.¹⁷

Chinese ODI in the EU is no exception. In a recent survey conducted by the European Chamber of Commerce in China, market seeking is found to be the principal motive for Chinese investment in the EU by a wide margin (European Chamber 2013, 13). Similarly, a survey by Deloitte (2007) on emerging countries' direct investment in Germany finds that geographical expansion is a key objective ahead of access to technology (10).

(Figure 1 about here)

Market access may be gained through greenfield investments as well as through M&As. Teaming up with a well-established firm is seen as a way of gaining quick access to the EU market. Joint ventures negotiated by Chinese firms in the telecommunications industry

¹⁷ See, for instance, Yao, Yang, and Yin He (2005) or IBM Consulting Services (2005). Similarly, a survey of China's 50 largest 'industry-leading' firms by Roland Berger (quoted in Wu 2007) found that 56% of Chinese investors cited 'seeking new markets' as the main motive for their investment, compared to only 16% for 'obtaining technology and brands'. For econometric testing, see for instance Buckley et al. (2007).

are obvious examples of this strategy. Similarly, through the acquisition of French Le Cabanon/Conserves de Provence, the Chinese investor Chalkis was seeking to get access to a well-developed distribution network in the European market. The same holds true for Shanghai-based Bright Food Group's purchase of a 60% stake in British cereal maker Weetabix Ltd in May 2012.

Strategic asset seeking is the second most important reason for Chinese ODI in Europe. Whatever the form, the acquisition goals seem to be access to a brand name and distribution network¹⁸ or to engineering know-how and customer networks.¹⁹

The choice of country is partly opportunistic – such as when an acquisition target becomes available – and partly a reflection of the different strategies behind Chinese ODI in Europe. Although each country has attracted firms from several sectors, there does seem to be a tendency to invest in those sectors for which the host-country has a particular strength: machinery in Germany,²⁰ design in Italy and, to a lesser extent, the automobile sector in the UK.²¹ This does suggest a desire on the part of investors to obtain strategic assets from their European acquisitions. In such cases, the deals result from the coincidence of a supply of know-how and financial difficulties on the one hand and financial strength and demand for technical expertise on the other.

The link between location choices and technology sourcing is even more apparent when it comes to R&D centers. The location of some Chinese investments in developed economies is clearly indicative of their aim to capture high tech human capital and to benefit

¹⁸ TCL's acquisitions of Schneider and Thomson are obvious examples of these goals.

¹⁹ These goals were evident in numerous acquisitions of German firms in the machinery and metal industries such as Welz, Lutz Schiess, and more recently Putzmeister.

²⁰ Shenyang Group, Huapeng Trading, Dalian Machine, and Sany Group among others.

²¹ Nanjing Automotive and Huaxiang Group.

from economies of scale of Marshallian districts (UNCTAD 2003, 6).²² This strategy is exemplified by the investment by Chinese telecom equipment firm, Huawei, in a R&D facility in Sweden and by Haier investing in Germany. Similarly, JAC Anhui Jianghuai established itself in Turin to benefit from the proximity to the Moncalieri science and technology parks.

Of course the motivations may vary among Chinese investors. While SMEs search for new business opportunities in low-tech manufacturing, China's emerging champions such as Huawei and ZTE seek to improve their market position abroad, to diversify their activities and to acquire new technologies (Apoteker, Barthélémy, and Lunven 2013).

Much is made in the academic literature about how the strategic-asset seeking nature of Chinese investment sets it apart from earlier waves of ODI by American, European and Japanese firms. Deng (2007) encapsulates this point of view when he argues that 'Chinese... [multinational corporations] are motivated primarily by the quest for strategic resources and capabilities, and...the underlying rationale for such asset-seeking FDI is strategic needs' (71). Rugman and Li (2007) take the opposing view by arguing that 'only to a minor extent do MNEs [multinational enterprises] go abroad to gain access to knowledge and technology' (341).

Without wishing to add to the voluminous literature that this debate has spawned, it is nevertheless useful to point out two empirical facts. First, surveys of investor motives continue to give only a secondary role to strategic-asset seeking, even for Chinese investments in Europe (and incidentally, North America as well). Secondly, to the extent that strategic-asset seeking motives exist, many studies have found similar motives for earlier Asian investments in Europe and the United States, as well as for European investments

²² So-called Marshallian districts accommodate a large number of small firms producing similar goods to be exported, and benefit from the accumulation of know-how associated with workers residing there. They are further characterized by high labor mobility.

overseas. Chinese ODI might be unusual, even surprising, but China is still on the same planet as the rest of the world.

All these remarks also suggest that the role of the state should not be overblown. Chinese ODI undoubtedly benefits from easy finance provided by the Chinese government, but the strategies followed by Chinese investors are primarily based on commercial and economic considerations.²³ It would thus be a major mistake to assume that all investments belong to a grand strategy designed in Beijing. Actually, as Freeman (2013) explains, the propensity of Chinese enterprises (even SOEs) to evade or ignore government regulations and policy is such that drawing simple causal relationships between government policy and behavior of Chinese firms is fraught with difficulty (14).

3.3. Pull and Push Factors

On top of these broad strategies are various push and pull factors that encourage Chinese firms to venture abroad. They help to explain why investing is preferred to exporting or Original Equipment Manufacturing (OEM) sales to foreign investors and why Chinese firms from so many sectors are deciding to invest in so many countries at the same time. These push and pull factors are obviously inter-related.

Pull Factors

The decision to invest rather than export is sometimes precipitated by actual or threatened protectionism in major markets. The record Chinese trade surplus with the EU has no doubt raised the sensitivity of Chinese exporters to this potential threat. For instance TCL's purchase of Schneider Electronics in Germany arose partly in order to circumvent European

²³ Government support, through hidden subsidies and cheap financing, gives Chinese SOEs a clear advantage over their competitors.

import quotas.

In addition, the latest EU enlargements in 2004 and 2007²⁴ have attracted Chinese firms to lower-cost locations and allowed them to get easy access to the rest of the EU (Filippov and Saebi 2008, 19). The perceived advantages of moving production to the New Member States lie in the proximity of these states to Western Europe and in their cost structure.

Of course, the recent euro-debt crisis has probably provided an additional reason for Chinese investors to move to the EU, as a number of European firms are in financial distress. However, this motivation should not be overestimated: Chinese investors targeted ailing or financially distressed firms even before the debt crisis. The conditions may now be more attractive as these firms are available at discounted prices, but this should be interpreted as a facilitating factor rather than an entirely new motivation.

Push Factors

Chinese government policies play an important role in Chinese ODI, not necessarily through their active encouragement of it but through liberalization of the outward investment regime and the easing of foreign exchange restrictions. Another aspect of this liberalization is the commitments by China as part of its accession to the World Trade Organization in 2001. Chinese firms in many sectors are now facing much greater competition in their domestic market, placing downward pressure on profit margins at home.

Overcapacity and high market shares at home encourage Chinese firms to look abroad for future earnings growth. Cheng and Stough (2007) consider overcapacity and falling prices

²⁴ In the wake of the collapse of the Soviet block, 10 countries joined the EU in 2004 (Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia). Bulgaria and Romania joined in 2007.

as the main motive for market-seeking ODI by Chinese MNEs. Almost half of the respondents in a McKinsey survey of Chinese MNEs said that they were pushed to globalize by increased domestic competition (McKinsey 2008, 9).

3.4. Impacts of Chinese Investment on European Economies

Chinese investment in the EU is part of a broader phenomenon, namely the reemergence of major markets such as India and China after a long period of quasi-autarky, which will have profound implications for European firms and workers, producers and consumers. By itself, however, Chinese ODI is more a manifestation of these changes than a driving force behind them. The arrival of firms from China and other emerging markets in Europe poses threats and opportunities for host countries, but its overall impact might well be indistinguishable from what is already occurring through trade.

Concerning job creation or preservation, any effect on the acquired firm must also be assessed against an appropriate counterfactual: what would have happened to production in Europe in the absence of the acquisition? In many cases, the acquired firm was either bankrupt or facing severe financial difficulties. Overall, the employment impact of Chinese ODI can be expected to be limited at the aggregate level because of its still-small size, although local implications may not be negligible. In this respect, the picture is rather mixed with a combination of failures involving plant shutdowns and job losses where ailing firms could not be turned around, and on the other hand, success stories associated with plant expansion and job creation. Overall, however, the impact in terms of job creation or preservation is relatively modest because Chinese ODI tends to be concentrated in sectors that are not labor-intensive. As highlighted earlier, the bulk of Chinese ODI is in the tertiary sector, with a particular emphasis on trading activities and the establishment of representative

offices that aim to provide support for exports. Similarly, R&D centers do not tend to generate many jobs.

While it is not uncommon for Chinese investors to put an end to labor-intensive production in Europe and move it to China, in some cases productive activities are taken up again on European sites after a temporary interruption. Such was the case of Nanjing Automobile, which started by transferring production to China and shifted it back to the UK two years later. Thus there is no general rule, and industrial activities are not systematically relocated to China. In some other cases still, Chinese investors opt for the duplication of production in Europe and China since having a presence in Europe is a way for Chinese investors to acquire expertise that can eventually be exploited in the fast expanding Chinese market (such has been the case of China BlueStar for instance).

Turning now to the impact of Chinese ODI on host countries' industrial structure, the major lesson is that the chances for the revival of sunset industries are rather bleak as exemplified by repeated failures in the acquisition of television production units (Thomson, Schneider, and Novel Vision are instances of this). Although they may provide a much-needed capital infusion, Chinese firms have not been particularly successful at turning European companies around. Successful takeovers arise mostly where there are synergies between the two partners, with the Chinese investor providing more than just cash but also competitiveness in a given area. According to Hay et al. (2008), the impact of Chinese ODI differs across countries, with German industries emerging stronger thanks to Chinese investment, while French industrial weaknesses are in contrast deepened (11). As explained earlier, this difference has to do with the different sectoral specialization of Chinese investments in these two countries.

The arrival of Chinese investors may also intensify competition in some sectors, with positive as well as negative effects depending on local producers' ability to adjust. For

instance, the penetration of Chinese operators in the telecommunications equipment industry has intensified competition in Europe and stimulated local producers.

Indirect positive spillovers should also not be underestimated. First, there is the possibility for European firms to profitably discharge underperforming assets or to benefit from much needed capital injections. Secondly, Chinese investors may also provide higher returns for European investment in R&D as they often pay premium prices for western technologies embedded within European firms. Lastly, and more importantly, the participation of Chinese investors in European companies' capital may be instrumental in helping the latter gain access to the still relatively closed Chinese market.

Despite these various positive impacts, there are also risks and challenges from Chinese ODI in Europe:

- in some sectors, Chinese investors represent a genuine competitive threat to European firms especially as they become more adept at managing brands and catering to European tastes;
- corporate governance among investing firms is often weak, stemming from a lack of transparency, poor accountability, and close ties with the Chinese government;
- lack of transparency, which is particularly acute for SWFs;
- subsidized Chinese SOEs may represent unfair competition for European rivals;
- European firms may not enjoy the same ability to acquire Chinese firms as Chinese investors have in Europe;
- national security concerns arise from the possible leakage of critical European technologies to China.

4. European Responses to the Chinese Economic Presence

4.1. The Context: Tighter Restrictions Increasingly Popular Worldwide

The evolving global investment landscape and the rise of state-backed direct investors from emerging countries (in particular China and Russia) have implications for investment policymaking. On the whole, countries have been revisiting their stance on investment policy and have shifted from liberalization to more regulation. The point of the newly revised laws is to restrict certain types of FDI or to expand government oversight of cross-border investments. Most of these measures have been justified on the basis of protecting national security or safeguarding so-called strategic industries. As explained by the OECD:

[F]rom France and Germany, the United States and Canada, to various non-OECD countries, existing regulatory regimes have been used to deter certain investments in infrastructure for national security concerns or countries have tightened their regulations on security grounds (OECD 2007, 55).

To that end, some countries have established new national security review processes for foreign investment or created additional tools for scrutinizing acquisitions by government-owned companies and/or SWFs (Marchik and Slaughter 2008, 2).

In the US, the Committee on Foreign Investment in the United States (CFIUS) is in charge of reviewing transactions that could result in control of a US business by a foreign person (so-called ‘covered transactions’).²⁵ The review seeks to determine the effect of such transactions on US national security. Existing regulations were amended in 2007 during President George W. Bush’s administration by the new Foreign Investment and National

²⁵ The CFIUS was created in 1988 with the Exon-Florio amendment to the Omnibus Trade and Competitiveness Act (P.L. 100-418, Title V, Subtitle A, Part II, or 50 U.S.C. app 2170).

Security Act (FINSA), bringing about major changes.²⁶ First, the meaning of ‘national security’ has been fundamentally expanded to include critical infrastructure and homeland security as areas of concern comparable to national security. Secondly, the CFIUS is now required to investigate all foreign investment transactions in which the foreign entity is owned or controlled by a foreign government, regardless of the nature of the business.

Interestingly, China has also recently (in August 2011) adopted a national security review mechanism allowing the Chinese government to review mergers and acquisitions of domestic companies by foreign investors for national security purposes. In China, one of the criteria for assessing inbound investment is ‘economic security’.

While European countries still purport to promote FDI inflows, they have also tended to individually move towards more regulation or restrictive policy measures. This conflicting approach to policymaking is increasingly prevalent and can be seen as a result of the concerns raised by the sharp rise in Chinese ODI. This rise has sparked a debate in the EU about the need to establish a mechanism for vetting foreign investment similar to that which exists in the US. Another oft-heard argument is that the EU should respond to China’s recent enactment of its national security review mechanism.

After a brief reminder of the EU regulatory framework, the following section examines the terms of the debate on a new EU investment policy vis-à-vis China.

4.2. The Regulatory Framework: National Provisions under EU Control

In the EU, the regulation of inward FDI used to result from three main legal frameworks: the

²⁶ This was, in part, a response to the failed attempts by the Chinese company CNOOC to acquire the US oil company Unocal in 2005, and Dubai Ports World to manage six US ports in 2006 (Watai 2013).

Treaty on the Functioning of the European Union (TFEU);²⁷ national laws on foreign investment; and so-called ‘Bilateral Investment Treaties’ (BITs) that address post-establishment protection issues.

The Treaty on the Functioning of the EU

The TFEU lays out how the EU operates. The general principle of free capital movement *erga omnes* (that applies both within the EU and vis-à-vis non-EU investors) is stated in article 63 of the TFEU according to which ‘all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited’.

However, under articles 64 and 65, EU member states retain the right to depart from the principle of free movement of capital and to take restrictive measures that are justified on grounds of public policy or public security, as long as ‘those restrictions do not result in arbitrary discrimination or a disguised restriction on trade’. This is further confirmed in article 346 regarding the possibility of taking measures necessary for the protection of a country’s essential security interests. In a nutshell, each country may regulate FDI inflows as it sees fit, provided it does not depart from the rules set out in the TFEU.

The European Commission (which is the body charged with overarching coordination and regulation of the EU) generally seeks to prevent member states from blocking acquisitions for protectionist reasons. Moreover, the interpretation of what constitutes a public security issue is restrictive and the jurisprudence of the EU Court of Justice has imposed tight

²⁷ The TFEU goes into detail on the role, policies and operation of the EU. The latest consolidated version after the Treaty of Lisbon came into force is available at:
<http://register.consilium.europa.eu/pdf/en/08/st06/st06655-re07.en08.pdf>.

limitations on possible derogations from the *erga omnes* principle, in particular regarding the use by member countries of ‘golden shares’ (Sautenet 2012).²⁸

National Provisions

Although European public opinion tends to be generally critical of the potential benefits of FDI coming from countries such as China, European governments tend to favor inward FDI flows through various measures aimed at enhancing their country’s attractiveness.²⁹ All European governments have set up economic development agencies (examples include Germany Trade and Invest, Invest in France, and UK Trade and Investment) that have the objective of supporting foreign companies wishing to establish themselves in the country by providing them with assistance ranging from market entry to business start-up. The ultimate aim is to increase the number of job creations in the country. The recent global financial crisis has even led to rising competition between European countries for inward FDI.

Of course this openness to FDI inflows does not mean that there is no control over the type of direct investments made. Although public authorities may see incoming FDI flows as a way of boosting domestic activity, they also have to create conditions that minimize the risks and maximize the benefits associated with these flows. Over the past few years, the major EU countries have reformed their policy on inward FDI so as to make it more

²⁸ A golden share holds special voting rights, giving its holder the ability to block another shareholder from taking more than a ratio of ordinary shares. They are popular with governments wishing to maintain control over privatized firms. In the EU, golden shares have been deemed illegal.

²⁹ During his trip to Beijing in April 2013, President François Hollande explained that France was open for business, and publicly called for more Chinese investments to be made (2013. “François Hollande prêt à lever tous les freins aux investissements chinois en France.” *Le Monde*, April 26).

restrictive, sometimes leading to conflicts with the TFEU.³⁰ The restrictions do not, however, target any investors in particular.

With regard to China, European countries have adopted an inherently ambivalent approach. On the one hand, European governments are tempted to protect their producers from rising competition from China and to avoid the takeover of some so-called strategic activities by foreign interests. On the other hand, they are also willing to maintain their countries' attractiveness in order to preserve jobs and maximize the chance of strong and stable economic growth. As Meunier (2012) aptly puts it, 'the difficulty is in finding the right balance between ensuring the benefits from Chinese FDI, from job creation to productivity gains, while protecting from its harmful effects' (iii). The responses have so far been restricted to the national (as opposed to EU-wide) level.

Germany

Because Germany is an export-oriented economy, keeping its doors open to foreign investment is important in order to avoid any protectionist backlash and to maintain access to foreign markets such as China. As a result, Germany has retained a very open attitude to foreign investments, and particularly those coming from China. The financial difficulties encountered by a number of medium-sized German firms have also encouraged the government to maintain a liberal stance. The German policy is entirely non-discriminatory and treats all investors in the same way irrespective of their country of origin, their sector of activity, and the magnitude of their investment.

Until recently, Germany limited its control of foreign investments to armaments manufacturers. However, German politicians have grown increasingly concerned about

³⁰ As reported by the OECD (2013), over the period 2008–2013, five EU members amended their investment policies with respect to national security (6).

investments by SWFs and SOEs. In 2007, apparently in response to the announcement by CIC that it would start investing abroad, a debate began in Germany about the need to tighten the laws concerning investment controls. In 2008, the German government amended the German Foreign Trade and Payments Act and regulations (*Aussenwirtschaftsgesetz* and *Aussenwirtschaftsverordnung*)³¹ thereby authorizing the Ministry of Economics and Technology (together with other German ministries) to review and possibly block certain foreign (i.e., non-EU) investments, particularly those by SOEs. According to the legislation, FDI may be subject to a new investment screening process if at least 25% of the voting rights in a German company are acquired by a foreign (non-EU) investor. The investment may be blocked if it poses a threat to ‘public order and security’ in Germany. The procedure complements an existing review procedure that addresses only investments in certain military goods and cryptographic equipment; the new procedure is not limited to specific industries.

France

In France, in line with the TFEU, the general principle of free movement of capital is stated in article L 151.1 of the Monetary and Financial Code (Code Monétaire et Financier). However, the French government retains the right to depart from this principle under specific conditions. The rules on so-called ‘sensitive investments’ are contained in the articles R 153 sq. of the Monetary and Financial Code revised in May 2012.³²

The revised regime introduces a distinction between FDI inflows from other EU countries (as well as from the European Economic Space) and those from outside the EU,

³¹ Dreizehntes Gesetz zur Änderung des Außenwirtschaftsgesetzes und der Außenwirtschaftsverordnung.

³² Decree n°2012-691 du 7 mai 2012 relatif aux investissements étrangers soumis à autorisation préalable.

with a less restrictive regime applicable to the former. In addition, it identifies 11 specific sectors that may affect ‘the national interest’ and in which foreign investments are subject to prior approval by the Ministry of Economy and Finance. Four of these sectors are defense-related and the seven others are public order-related. Because the sensitive sectors are precisely defined, the degree of discretion left to public authorities is rather limited and the resulting transparency is a way of limiting uncertainty for foreign investors.

Although the percentage of the investor that is owned by a foreign government would be taken into consideration in the investment review process, France does not have any laws or policies that specifically restrict SOEs or SWFs from investing in France.

The UK

The UK has historically maintained a very liberal investment policy. In contrast to France and Germany, the UK does not have a regulation that specifically deals with FDI alone. However, other regulatory mechanisms such as the Enterprise Act (2002), which regulates anti-competitive behavior, allow for indirect control over FDI. The Act grants the government the authority to intervene to block or place conditions on the approval of M&As involving British companies if the transaction is considered to be contrary to the public interest.

Austria

Austria has recently introduced a screening system for national security. The new Austrian Foreign Trade Law,³³ which came into effect on 8 December 2011, establishes a review mechanism for foreign investment in Austrian companies that operate in sectors sensitive to public security and order. In particular, it requires that foreign investors from countries

³³ Außenwirtschaftsgesetz 2011, BGBl. I Nr. 112/2011.

outside the EU and the EFTA seek authorization from the Ministry of Economy for investments that would lead to ownership or voting rights of over 25% in companies with a seat in Austria operating in certain sectors. These sectors include defense and security, hospitals, rescue and fire-fighters, crisis-prevention, power generation and distribution, natural gas and water distribution, telecommunications, transport and traffic by land, air or waterways, as well as the education sector including universities, schools, and kindergartens (OECD 2013, 14).

Italy

On 9 March 2012 the Italian Government approved a Law Decree³⁴ establishing for the first time a review mechanism for transactions involving assets of companies operating in the sectors of defense or national security, as well as in strategic activities in the energy, transportation and communications sectors. The new rules include specific governmental powers to veto corporate transactions that trigger a threat of severe prejudice to the essential interests of the State. The law further sets out the authorities that carry out the risk assessment and the criteria to follow, and defines timeframes and obligations on companies to provide information to the government about the investment project.

The law also abolishes the former Italian Golden Share Law (No 474 of 1994), which the European Commission had deemed to contravene European Law.

³⁴ Law of 11 May 2012, n. 56, Gazzetta Ufficiale della Repubblica italiana n. 111 del 14 maggio 2012.

The Netherlands

The Netherlands' trade and investment policies are among the most liberal in the world. The Netherlands possesses no review process for foreign investment, and according to Dutch government officials, the Netherlands in fact lacks the general authority to block investment. Foreign and domestic companies are treated equally under Dutch law, and regulations for M&As apply to domestic as well as foreign investment. Foreign investment, like domestic investment, must go through an anti-trust review. However, according to government officials these reviews do not provide the Dutch government the authority to block investment on national security grounds. The one exception is in the financial sector, where the Netherlands Central Bank, and in some cases the Finance Minister, can block M&As (Government Accountability Office 2008, 80-84).

Bilateral Investment Treaties

In general, BITs are used in order to promote and attract foreign investments by granting them protection once they are established. Until the Lisbon Treaty,³⁵ investment was an area of mixed competence: while the EU was in charge of some investment-related negotiations in the form of International Investment Agreements (IIAs), the individual member states signed BITs primarily to protect the interests of their investors abroad.

Under the Lisbon Treaty, in addition to its exclusive competency to negotiate trade agreements, the European Commission is entitled to negotiate international investment rules. In other words, the EU's investment power now comprises both the pre-establishment as well as the post-establishment phase.

³⁵ Treaty of Lisbon amending the Treaty on European Union and the Treaty Establishing the European Community, signed at Lisbon, 13 December 2007, Official Journal of the European Union, Volume 50, 17 December 2007.

4.3. Towards a Common Investment Policy Under China's Pressure?

The State of the Debate

At the EU level, a number of instruments are in place to protect EU economic interests against rising competition from foreign investors. Such frameworks encompass competition policy reviews, labor regulations and transparency requirements. However, a widely-held view argues that this is no longer sufficient in the context of rising FDI from emerging economies, which have objectives that may not be commercial and as a result may potentially threaten national interests (Röller and Véron 2008, 7). To be more specific, there is growing concern in the EU regarding investment by Chinese SOEs and SWFs.

The coexistence of fragmented national approaches highlighted in the foregoing section and the lack of consistency between existing regulations constitutes a major weakness for the EU. These regulatory disparities may be taken advantage of by foreign investors and/or may be a source of conflict within the EU. With the rise of Chinese investments that presumably stand if not under the control, at least under the influence of, the Chinese government, a number of European countries have called for a common concept of national security and a supranational framework for screening foreign investment for security threats (Godement and Parelo-Plessner 2011, 10). The need to create an EU-wide review mechanism is considered to be all the more desirable since such a mechanism is in place in China, thus creating a clear asymmetry in the conditions of market access by EU firms in China and by Chinese firms in the EU. Moreover, now that investment issues fall under the remit of the EU rather than of individual member states, it seems logical that the EU should regulate inbound foreign investment on behalf of member states.

With respect to post-establishment issues, the negotiation of a single BIT between the EU and China is also perceived as necessary now that such deals fall under the remit of the European Commission. Moving in this direction is deemed to be all the more desirable since

most of the existing 27 BITs (with all member states except Ireland) were initially negotiated in the 1980s when China was only a recipient of foreign direct investment. Now, as a foreign direct investment exporter, China is likely to be more willing to offer broader protection of investment and investors.

An EU-Wide Review Mechanism: Mission Impossible?

A discussion was first started in 2008 regarding a common European approach to regulating investment by SWFs (Röller, Hendryk, and Véron 2008, 2). The result was the publication of a communication by the EU Commission (European Commission 2008). The core message of that communication was that establishing an EU committee on foreign investments similar to the CFIUS in the US – or creating an EU-wide screening mechanism or some ‘golden shares’ mechanism for non-EU foreign investment – would run the risk of sending the misleading signal that the EU is stepping back from its commitment to an open investment regime. The communication also suggested that such arrangements would be difficult to reconcile with EU law and international obligations.

A couple of years later, however, following the unsuccessful attempt by Chinese cable-maker Xinmao to acquire the Dutch fiber-cable producer Draka in 2010, a new debate was triggered by two EU Commissioners (Antonio Tajani, Industry, and Michel Barnier, Internal Market and Services). The Commissioners called for an EU-wide foreign investment review regime to protect European know-how and technology from foreign investors.³⁶ The fear was that foreign companies could get hold of technology that could then become inaccessible in Europe, or could gain control of infrastructure, which they could then block or switch off. The proposal reflected widespread European concerns about China, but can also be

³⁶ ‘You need fire insurance before there's actually a fire’, Tajani said in an interview, ‘It's not protectionism, it's being careful’ (quoted in Miller, 2011).

seen as an attempt to use investment controls to restrain competition. No concrete result emerged from this episode, and the issue is currently being discussed again by two EU Directorates (Trade and Internal Market).

Given the diverse nature of the EU, an EU-wide body to vet foreign investments will not be easy to come by. First, it could not be a functional equivalent of the CFIUS because the EU is not a state but a market. As a result, national security (encompassing both national defense and public security) falls under the purview of individual sovereign states. Secondly, the perceptions of competition vary widely across countries with some countries being negatively affected while some others are in a better position to resist competitive pressures from foreign investors. Thirdly, and as a corollary of the previous point, the diversity of reactions to the Commissioners' aforementioned proposal shows how deep the differences are among European policymakers over managing foreign investment flows. Lastly, should European countries concur on the need to adopt a common stance, they may not easily agree on the definition of a list of strategic sectors where foreign investment ought to be restricted or entirely prohibited. Such a list could include sectors that are deemed to need special protection or sensitive sectors for defense and security, but even these concepts are not necessarily widely shared.

Rather than an EU-wide review mechanism, another (alternative or rather complementary) avenue is to strengthen the monitoring of foreign investment on the grounds of competition policy (which is an EU competence). This would have particular application to the case of China, given the great number of investment deals proposed by state-owned companies (Meunier 2012, 9). However, such a move is unlikely to be enough because it would merely solve part of the potential problems. An additional effort at coordinating national policies is definitely needed.

As for the scope of the screening mechanism, it is the author's conviction that it should be kept to a minimum. In particular, the establishment of any form of review mechanism should not be based on an argument of negative reciprocity, which is the willingness to harm those who previously harmed you. Far to the contrary, positive reciprocity, or the willingness to return favors, should be the name of the game. As explained earlier, keeping the door open to Chinese investors is also a way of easing access to the Chinese market for companies collaborating with Chinese partners. An approach based on positive reciprocity implies that the restrictions imposed on Chinese investors should encompass purely national security considerations and exclude economic security issues.

A China – EU Investment Treaty

Prior to the Lisbon Treaty of 2009, post-establishment issues were regulated through BITs concluded by individual member-states with the main objective of ensuring that European investments abroad would be protected against risks of expropriation and discrimination by host countries.

Since the Lisbon Treaty, regulation of foreign direct investment coming to (and leaving) the EU is an exclusive competence of the European institutions and no longer of the member-states. This is why on 23 May 2013, the European Commission decided 'to ask the member-states for their agreement on a mandate to open negotiations on an investment treaty with China'.³⁷ Once the mandate has been agreed upon by the European Council,³⁸ the Commission hopes to start negotiations shortly. Such a deal would be the first since the Lisbon Treaty came into force.

³⁷ <http://trade.ec.europa.eu/doclib/press/index.cfm?id=900>.

³⁸ The European Council comprises the heads of state or government of the member-states of the European Union.

From an administrative and legal point of view, such an agreement would have the advantage of streamlining all the existing bilateral agreements with China into one comprehensive set of rules to be followed for investment by all European countries. The Commission also hopes that the negotiations will be an occasion to discuss in-depth the issues that European companies face when operating in China. For instance, the Commission wishes to reduce discriminatory practices, especially in the form of mandatory joint-ventures. On such an issue, positive reciprocity may prove particularly appropriate and this is why keeping Europe open to Chinese firms should be a key objective. The European Parliament, which also has a say in such a negotiation under the Lisbon treaty,³⁹ also stresses that the deal must deliver greater equality between the two partners' investment environments.

Reactions to the Commission's plans have so far been few and sparse. It is highly plausible that a more substantial debate will take place in the national capitals once the talks have begun and real proposals are on the table. However, a substantial degree of convergence is likely to be achieved among EU member-states because most of them have an interest in getting better access to the Chinese market for their firms. The negotiation of a single BIT will also contribute to the EU's emergence as an FDI actor in its own right, thus enhancing its bargaining capacity.

The negotiation will not be an easy one; the liberalization of market access (an area that was not covered by traditional BITs) as well as the creation of a bilateral dispute settlement mechanism can be expected to emerge as the most contentious issues between the two parties.

It is said that China would have preferred to begin talks on a fully fledged free-trade agreement of the sort that the EU is contemplating with the US. European officials, however, seem to prefer a step-by-step approach. They have indicated that if the investment agreement

³⁹ Once the deal is struck, Parliament's consent will be needed in order for it to enter into force.

can be concluded and made to work, then further talks on broader issues can be considered.

The fact that the BIT may be seen as a first step can (and should) also be used as a bargaining chip by the EU.

5. Conclusion

Although Chinese ODI into the EU remains limited and such capital flows are not unprecedented, the challenges posed are often perceived to be of a different kind because of the unique nature of the Chinese regime and the allegedly large role played by state-related players such as SOEs and the various Chinese SWFs (CIC and SAFE in particular). A thorough examination of the current situation suggests, however, that there is a substantial gap between the account provided by the media and the reality of Chinese direct investment in the EU. Moreover, so far there has not been a single problematic case when an acquisition by a Chinese investor may have posed a risk to national or European security. In this context, the challenges posed by the recent influx of Chinese ODI should not be overblown and public pressure to restrict such influx for political reasons should be resisted.

Nonetheless, repeated concerns about Chinese foreign investment as reported in the press do create the risk of a protectionist drift inside the EU. Also, the possibility that some investors may one day pose a threat to national security cannot be fully ruled out. As a result, the current situation characterized by a fragmented approach cannot be deemed satisfactory and a more consistent legal framework is called for. Recent experiences suggest that the establishment of a common EU-wide review mechanism may be overly complex. This leaves better coordination of national policies under the guidance of the EU Commission, as well as a more systematic and coordinated use of existing mechanisms such as competition policy, as the most realistic options. Also, pushing for the negotiation of a China-EU BIT is certainly a

promising avenue to enhance the EU's bargaining leverage based on the principle of positive reciprocity.

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Table 1. A selection of M&As by Chinese Investors in the EU.

Activity	Buyer and Seller, Country	Date	Amount (US \$mil) (%)
Mining	Zijin Mining Group – Monterrico Metals, UK	2007	186
	Zijin Mining Group – Ridge Mining, UK	2006	15.9 (29.9%)
	China Guangdong Nuclear Power – Kalahari Minerals	2012	1000
Food	Chalkis – Le Cabanon/Conserves de Provence, France	2004	(55%, then 100%)
	CIC – Diageo, UK	2009	370 (1.10%)
Automotive	Fuyao Glass Industry Gp – Fürmotec GmbH, Germany	2007	N/A
	Geely – Volvo, Sweden	2010	1800 (100%)
	Weichai Power – Moteurs Baudouin, France	2009	6 (100%)
	Nanjing Automotive – MG Rover, UK	2005	85 (100%)
	Huaxiang – Lawrence Automotive, UK	2007	46
	Huaxiang Electronics Co – HIB Trim Part Solution, Germany	2013	38
	Qinjiang Group – Benelli, Italy	2005	N/A
Chemicals	China National Blue Star Group – Adisseo, France	2005	N/A (100%)
	China National Blue Star Group – Rhodia Silicone Division, France	2006	N/A (100%)
	China National Bluestar Group Corporation – Fibres Worldwide, UK	2007	N/A (100%)
	Shanghai Dongbao Biopharmaceutical – Ferring’s Malmö Factory, Sweden	2006	

Activity	Buyer and Seller, Country	Date	Amount (US \$mil) (%)	
Consumer Electronics	TCL – Schneider Electronics, Germany	2002	11 (100%)	
	TCL – Thomson, France	2003	N/A	
	Nam Tai Electronics – Stepmind, France	2004	7.75	
	Lenovo – Medion, Germany	2011	800 (100%)	
Household Appliances	Haier – Meneghetti Refrigerator, Italy	2001	8	
Machinery and Metal Products	LiuGong Machinery - Huta Stalowa Wola (HSW), Poland	2012	N/A (100%)	
	SHIG Weichai – Ferretti, Italy	2012	507 (75%)	
	Sany - Putzmeister, Germany	2012	500 (100%)	
	Shenyang Machine Tool Group – Schiess, Germany	2004	9.7 (100%)	
	Shenyang Heavy Machinery Group (SHMG) – NFM Technologies, France	2008	27 (70%)	
	Huapeng Trading – Welz Gas Cylinder, Germany	2003	1.5 (100)	
	Shanghai ZQ Tools Group – Lutz Maschinenbau, Germany	2003	N/A	
	SGSB Group – Dürrkopp Adler, Germany	2004	38 (100%)	
	Dalian Machine – Zimmermann, Germany	2005	N/A (70%)	
	Harbin Measuring and Cutting – Kelch GmbH, Germany	2005	N/A	
	China National Building Material Group – Rotortechnik, Germany	2007	12 (100%)	
	Beijing No1 Machine Tool – Waldrich Coburg (Herkules), Germany	2005	N/A	
	Textiles	Sail Star Shanghai – Boewe Textile Cleaning, Germany	2003	N/A

Activity	Buyer and Seller, Country	Date	Amount (US \$mil) (%)
Research	Suntar Membrane Technology – Hoechst, Germany	2005	N/A (50%)
Energy	Three Gorges Project Corporation – Energias de Portugal, Portugal	2011	3500 (21%)
	CIC – GDF Suez Exploration and Production Business, France	2011	3200 (30%)
	Sinopec – Talisman Energy, UK	2012	1500 (49%)
	PetroChina – Ineos Refining, UK	2011	1000 (50%)
Banking	China Development Bank – Barclays, UK	2007	3000 (3.1%)
	CIC – Apax Partners, UK	2010	960 (2.3%)
Utilities	CIC – Thames Water, UK	2012	(8.7%)
	Cosco – Cargo Terminal Piraeus, Greece	2008	
Telecommunication	CIC – Eutelsat Communications, France	2012	485 (7%)
Logistics	LinkGlobal Logistics – Parchim Airport, Germany	2007	50 (100%)
Leisure	Fosun - Club Méditerranée, France	2010	N/A (7.1%)

Source: Author's compilation.

Note: Acquisitions by SWFs are shown in bold characters.

Table 2. China's ODI stock into the EU, 2004 – 2010.

(US\$ millions)

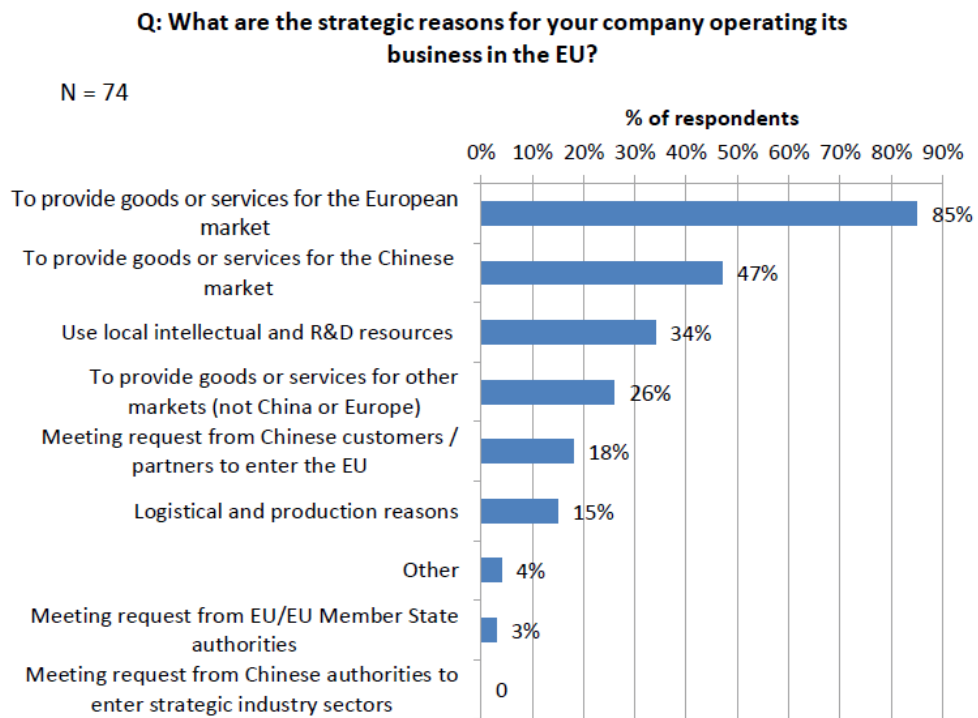
	2004	2006	2008	2009	2010
EU	553,2	1274,5	3173,9	6277,83	12496,9
United Kingdom	108,5	201,9	837,7	1028,3	1358,4
Germany	129,2	472,0	845,5	1082,2	1502,3
Sweden	6,4	20,0	157,6	111,9	1479,1
Spain	127,7	136,7	145,0	205,2	247,8
Netherlands	9,0	20,4	234,4	335,9	486,7
Italy	20,8	74,4	133,6	191,7	223,8
France	21,7	44,9	167,1	221,0	243,6
Poland	2,9	87,2	109,9	120,3	140,3
Hungary	5,4	53,7	88,8	97,4	465,7
Romania	31,1	65,6	85,7	93,3	125,0
Denmark	67,2	36,5	38,1	40,8	42,5
Belgium	1,6	2,7	33,3	56,9	101,0
Ireland	0,0	25,3	107,8	106,8	139,9
Czech Republic	1,1	14,7	32,4	49,3	52,3
Bulgaria	1,5	4,7	4,7	2,3	18,6
Other EU	19,1	13,8	152,3	2534,4	5870,0

Source: MOFCOM, *Statistical Bulletin of China's Outward Foreign Direct Investment*, various issues;

<http://english.mofcom.gov.cn/article/statistic/foreigninvestment>.

Note: Data for 2004 and 2006 include only non-financial ODI stock.

Figure 1. Chinese investors' motivations.



Source: European Chamber (2013); survey of 74 Chinese companies.