

European Parliament Briefing Paper

**POLITICAL IMPACT OF CHINESE FOREIGN DIRECT INVESTMENT  
IN THE EUROPEAN UNION ON TRANSATLANTIC RELATIONS**

Professor Sophie Meunier

Princeton University

Draft Prepared: 4 May 2012

(INTENTIONALLY BLANK)

## EXECUTIVE SUMMARY

This brief explores the political challenges posed by the recent influx of Chinese Outward Foreign Direct Investment (OFDI) into the EU and its potential implications for transatlantic relations. In spite of the media hype, Chinese direct investment is still minute in the EU, accounting for less than 1% of the total stock of FDI, but it is growing fast and the strong upward trajectory is likely to continue in the years to come. This surge represents challenges and opportunities for EU countries, not without historical precedent, but with novel threats as well. In the current context of economic and debt crisis in Europe, whether China is seen as a savior or a predator, the question of a Faustian bargain made by European countries by courting and hosting Chinese investment needs to be asked. On one hand, the benefits of FDI for the host economy are well known. On the other, Chinese OFDI may come with implicit strings attached and could potentially act as a Trojan Horse affecting European norms and policies, from human rights to labor laws. The surge of Chinese investment could also potentially affect European institutional processes, exerting both centrifugal and centripetal pressures on European integration. Finally, the influx of Chinese OFDI, which has risen faster in the EU than it has in the U.S., can create an unhealthy transatlantic competition with security ramifications, which should therefore be addressed. 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.

## **TABLE OF CONTENTS**

INTRODUCTION - 1

I. PATTERNS OF CHINESE DIRECT INVESTMENT IN THE EU - 2

1. Current patterns of Chinese OFDI in the EU

2. Potential trajectory of Chinese OFDI in the EU -3

II. FEARS AND OPPORTUNITIES OF CHINESE OFDI IN THE EU -4

1. Historical precedents

2. Yet novel challenges - 5

III. POTENTIAL POLITICAL IMPLICATIONS OF CHINESE OFDI IN THE EU - 6

1. Implications on foreign policy

2. Implications on domestic policy

IV. IMPACT OF CHINESE OFDI ON EUROPEAN INSTITUTIONAL PROCESSES - 8

1. Centrifugal pressures

2. Centripetal pressures

V. IMPACT OF CHINESE OFDI ON THE TRANSATLANTIC RELATIONSHIP - 10

1. Potential for different European and American trajectories

2. Potential for competition

3. Potential for cooperation

CONCLUSION - 11

ANNEX - 13

LIST OF ACRONYMS - 14

BIBLIOGRAPHY - 15

## INTRODUCTION

What do Volvo, the port of the Piraeus, and the Château Viaud vineyard and winery in Bordeaux have in common with Ferretti luxury yachts and Hungary's leading PVC manufacturer BorsodChem? They all belong to Chinese investors.

In addition to its massive holdings of debt in the United States and global portfolio investment through its sovereign wealth fund the China Investment Corporation (CIC), China is investing directly in real assets throughout the world, in industries from automobiles to zinc, in countries from Afghanistan to Zimbabwe. This investment is growing fast, in some cases exponentially, and is likely to continue to increase as Chinese firms are encouraged to go abroad by their government to diversify China's holdings and to obtain resources, technology, brands, managerial know-how and easier access to consumers.

Both in Europe and in the U.S., Chinese outward foreign direct investment (OFDI) is still minute, accounting for less than one percent of total FDI stock. But to European and American publics, reeling from what seems like a never-ending economic crisis and wary that the so-called "rise of the rest" is consecrating their own precipitous decline in power, it seems that Chinese companies are taking over and "buying up the world", as *The Economist* declared on its cover in 2010.<sup>1</sup> The longer the crisis in the Eurozone, the more it seems that China has its sights set particularly on Europe. This Chinese "scramble for Europe"<sup>2</sup> is a narrative consistent with the perceptions held by a majority of Europeans that China is already the world's largest economy.<sup>3</sup>

The actual or potential hosting of Chinese investment is viewed in Europe and the U.S. with ambiguity and trepidation. It represents simultaneously opportunity and menace. The security and economic implications of such investment are well known, but what about the political implications? Some people have called Chinese investment "dirty money" and compared accepting this money to prostitution. Does Chinese foreign direct investment indeed come with subtle conditions and potentially damaging strings attached, creating incentives for local actors to influence governments into changing their positions on a wide variety of foreign and domestic policies? Can these fears transform the institutional process dealing with and vetting FDI in the European Union (EU)? Will the competition to attract Chinese OFDI have a negative or positive impact on transatlantic relations? This report explores the potential political consequences of Chinese direct investment on European policies, institutions, and relations with the U.S.

---

<sup>1</sup> (The Economist, 2010)

<sup>2</sup> (Godement & Parello-Plesner, 2011)

<sup>3</sup>See Annex 1 (Pew Global Attitudes Project, 2011)

## I. PATTERNS OF CHINESE DIRECT INVESTMENT IN THE EU

According to the OECD and the European Court of Justice, direct investment is defined as a particular class of investment where the investor acquires at least 10% of the voting power of an enterprise, which establishes “lasting interest” and control over the affiliated company’s operations—in contrast to portfolio investment whereby investors do not generally expect to influence the management of the enterprise.<sup>4</sup> Contrary to the impression given by the proliferation of media reporting on instances of Chinese direct investment in Europe and the US, the actual volume of Chinese OFDI is minuscule. However, exploring its potential political implications is essential in light of its expected strong upward future trajectory, both because of the demand for and the supply of investment in the years to come.

### 1. Current patterns of Chinese OFDI in the EU

#### a. Volume

Chinese OFDI is growing fast: it doubled from 2.6% to 5.3% of GDP in the decade since China’s accession to the WTO in 2001<sup>5</sup>, with a total stock of \$364 billion worldwide<sup>6</sup>. But perceptions of China as an international investment juggernaut are greatly exaggerated. Indeed, it is the EU which is the world’s largest source and host of FDI. In spite of the hype, the volume of Chinese OFDI in the EU is minute.<sup>7</sup> It represents approximately 0.2% of the stock of FDI (versus EU investment accounting for 6.5% of the stock of FDI in China). If investment from Hong Kong is added to FDI from mainland China, it still amounts to about 1% of the EU’s FDI stock.<sup>8</sup> This is similar to patterns observed in the U.S., where Chinese FDI is also amounting to about 0.2% of FDI stock.

#### b. Nature

In Europe, as in the U.S., the majority of this investment has initially taken the form of greenfield projects –the creation of a factory or facility where none existed before—mostly setting up sales offices and distribution channels. But mergers and acquisitions (M&As) are growing fast and about to surpass greenfield projects.

#### c. Geographical distribution

Chinese OFDI is flowing mostly to Asia, and to a lesser extent Latin America and Africa, but Europe has been the fastest growing destination for Chinese investment since 2008. In

---

<sup>4</sup> (Organization for Economic Cooperation and Development, 2008)

<sup>5</sup> (A Capital, 2012)

<sup>6</sup> (Hanemann, 2012)

<sup>7</sup> Consistent and reliable statistics about Chinese FDI, in Europe and elsewhere, are difficult to gather. Depending on the sources and their calculation methods, numbers vary greatly. But data from the OFDI Chinese Statistical Bulletin, the U.S. Bureau of Economic Analysis, the Bertelsmann Foundation and the Rhodium Group’s “Chinese Investment Monitor” all point to a similar overall picture.

<sup>8</sup> (Xu, et al., 2012)

2010, Chinese OFDI into Europe and North America amounted to nearly 14 % of total Chinese FDI flows compared with just over 2 % two years earlier.<sup>9</sup> By some accounts, the EU even became the first destination for Chinese OFDI in 2011, with 34% of flows from China going to Europe.<sup>10</sup>

China now has investments in all EU member states. Great Britain and Germany are the first destinations for Chinese OFDI in the EU. In 2011, China surpassed the U.S. as the first direct investor in Germany.<sup>11</sup> Recently China has shown a particular interest in the countries of Central and Eastern Europe, starting with Hungary which received in 2010 more OFDI from China than all other CEE countries together.<sup>12</sup> In April 2012 China announced the creation of a new investment cooperation fund which would initially boast US\$500 million to assist Chinese investments in the CEE region. The rise of Chinese investment in CEE countries can be explained by a combination of CEE economies serving as a manufacturing base supplying Western Europe and the perception that the political climate is more conducive to Chinese investments than in Western Europe.<sup>13</sup>

#### d. Sectoral distribution

While resource acquisition has been a primary goal of Chinese OFDI across the world, in Europe Chinese companies have targeted the manufacturing sector and in particular the automotive industry (e.g. Geely's purchase of Volvo in Sweden, Great Wall Motors in Bulgaria, BYD automobiles in Hungary), industrial machinery (e.g. Sany's acquisition of Putzmeister in Germany), information and communication technology (e.g. Huawei in Hungary, China Unicom in the UK), and financial services (e.g. ICBC in the UK).

Increasingly, Chinese companies are showing an appetite for infrastructure projects that can build up chains of influence and help with distribution channels in Europe, such as ports (e.g. Piraeus in Greece, Rijeka in Croatia), airports (e.g. Parchim airport in Germany, Larnaca in Cyprus) and railways (e.g. in Slovenia and Hungary)

## 2. Potential trajectory of Chinese OFDI in the EU

The trend towards growing Chinese OFDI will likely continue upwards in the years to come. Chinese firms are projected to invest as much as \$2 trillion worldwide by 2020.<sup>14</sup> In the EU, that trajectory is likely to continue as well because of an increasing European demand for investment and an increasing Chinese supply of investment.

#### a. Demand for investment

---

<sup>9</sup> (Xu, et al., 2012)

<sup>10</sup> (A Capital, 2012)

<sup>11</sup> (Geitner, 2012)

<sup>12</sup> (Central and Eastern Europe Development Institute, 2012)

<sup>13</sup> See Annex 2 for a list of recent actual and proposed Chinese acquisitions in Europe.

<sup>14</sup> (Rosen & Hanemann, 2011)

The Eurozone crisis has left many countries scrambling for outside capital. All across the EU, governments are courting Chinese investment and setting up investment fairs to showcase their opportunities and attractiveness.

#### b. Supply of investment

For Chinese companies, investing abroad is not only a business decision but also a policy exhortation by the government to “go out”. Since 2000, China has encouraged its companies to develop operations overseas with preferential long-term government loans in order to “go global”. The 12<sup>th</sup> Five-Year plan (2011-15) has reaffirmed this objective, while streamlining and shortening the process for Chinese companies to invest overseas.

When it comes to the EU, the Chinese government has made clear that it was more interested in investing in real assets than in contributing to the Eurozone bailout fund, in part because Chinese citizens might not understand why their hard-earned money is used to finance the welfare states of Europe.<sup>15</sup> Therefore we will likely see a surge in Chinese direct investment in EU countries over the next few years as Chinese companies try to diversify their portfolio and optimize the return on investment.

EU countries can indeed provide Chinese companies with a lot of what they are looking for, above all the acquisition of brands and reputation, access to technology, qualified labor, access to infrastructure to facilitate trade, resources, and diversification of assets. It can also enable Chinese companies to circumvent future trade barriers in the case trade disputes turn into protectionist measures.

## II. FEARS AND OPPORTUNITIES OF CHINESE OFDI IN THE EU

The influx of Chinese capital has been encouraged by cash-strapped European governments burdened by the sovereign debt crisis in the Eurozone. Yet increasing Chinese penetration into European markets is instilling some fears among government elites and publics alike, and we might expect a few investment attempts to attract negative attention and to provoke public backlash, especially if Chinese investors acquire treasured assets and national icons.

### 1. Historical precedents

Political fears surrounding the influx of FDI have happened before. In Europe, a precedent is the “coca-colonization” by American multinationals which occurred from the 1960s on. Yet the best historical parallel is probably the explosion of OFDI from Japan into the U.S. in the late 1980s. Underscored by high-profile deals such as the 1989 purchase of Rockefeller Center by Mitsubishi Group, the conspicuous spike in Japanese OFDI took place against a political backdrop that bears striking similarity to that underlying Chinese investment

---

<sup>15</sup> (Geitner, 2012)

today: trade frictions, currency disputes, debates over state subsidies, and perceptions of economic threat and relative decline.

With the hindsight of both cases, we now know that on balance the consequences of FDI are positive: increased economic vitality and efficiency, creation and preservation of jobs, high-wage jobs, innovation and spillovers from R&D, and greater economic interdependence. Looking back at historical precedents suggests that Chinese OFDI will gain mainstream acceptance as it leads to economic growth, despite initial domestic political resistance.

## 2. Yet novel challenges

However Chinese OFDI also confronts Europe, as well as the U.S., with novel challenges without historical precedent.

### a. Developing countries investing in developed economies

The influx of Chinese OFDI is a novel situation for European countries more accustomed to investing in emerging, problematic economies than being treated like one of them. Throughout the 20th century, direct investment flowed almost exclusively from developed to developing economies. Europe and the United States were, and still are, the largest investors worldwide and the largest stakeholders in each others' economies. However, outward direct investment originating in developing countries exploded in the past decade, mainly in the direction of other emerging economies, such as India investing in Brazil or China in Africa. A much more recent phenomenon is that emerging countries, chief among them China, are now starting to invest in developed countries. Investing in Europe enables Chinese companies want to move up the global value chain but may be posing some “existential” political problems for some European politicians. Moreover, much of Chinese investment will likely be supportive of Chinese exports (through distribution, parts and service) and therefore may not create the type of well-paying jobs that FDI from rich countries has created and supported in the past.

### b. Communist regime investing in democratic countries

Another novelty is the nature of the political regime under which Chinese investors operate –the Soviet Union did not invest in the West. China’s authoritarian state and “capitalism with socialist characteristics” heightens sensitivity toward Chinese OFDI in Western democracies. While the full extent of the Communist party’s control of private and quasi-private firms in China is not clear, it is estimated that 66% of the stock of Chinese direct investment abroad comes from state-owned enterprises.<sup>16</sup> In many countries, a company’s investment abroad would be a purely commercial decision. In China, however, where the state owns a controlling interest in a variety of FDI-seeking companies, one can suspect that these companies are acting to fulfill strategic, rather than profit-maximizing, goals.

---

<sup>16</sup> (Xu, et al., 2012)

### c. Security rival investing in non-allied countries

The security environment also poses a novel challenge. China is both a potential military rival, as well as a heavy investor in “rogue” states such as North Korea and Iran. One concern is that Chinese OFDI in certain sectors runs the risk of enabling commercial and state espionage and creates the possibility of dual-use technologies transferring into the hands of the People’s Liberation Army or pariah regimes. A second concern is that, contrary to historical precedents, the flow of technology has so far been rather unidirectional, with the investors learning the technology in the host country and exporting it back to China, instead of bringing in technology along with the investment. A third concern is that European countries will become dependent on Chinese investment, which could provide China with political and security leverage. Worries therefore exist about Chinese OFDI, which carry particular significance because of China’s non-market economy, pattern of economic espionage, and poor track record with national security and human rights.

So the recent explosion of Chinese outward foreign direct investment presents a complicated dilemma for European policymakers. On the one hand, Chinese acquisitions have the exciting potential to improve and perhaps save struggling European companies, benefitting employees, shareholders, and local economies. On the other hand, Chinese investment comes with several national security concerns and without a guarantee to provide the above benefits.

### III. POTENTIAL POLITICAL IMPLICATIONS OF CHINESE OFDI IN THE EU

The combination of the global financial crisis, the massive accumulation of currency reserves, and the sovereign debt crises in Europe has turned China into a potential savior, seemingly dropping “helicopter money” in national economies that have few alternative prospects of cash influx, but also into a potential predator. In this scenario, China begins by preying on the weaker EU countries before insidiously penetrating the rich European economies, using direct investment as part of its master plan to take over the world. In any case, whether China is seen as a *deus ex machina* or a devil to whom weak European economies have sold their souls, the increasing willingness of Chinese entities to invest in Europe, directly and indirectly, raises the question of a Faustian bargain. Is Chinese investment buying more than goodwill?

The narrative of being taken over by China stokes preexisting fears about sovereignty and the decline of the West. French sovereigntist 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.*”<sup>17</sup> But various statements by Chinese investors lend credence to the idea that FDI might be an instrument of coercion to extract policy concessions from European governments and to transform the nature of Europe,

---

<sup>17</sup> (Lauter, 2011)

such as Cosco chairman Wei Jiafu's declaration that *"by going global, we are also transferring our culture to the rest of the world"*.<sup>18</sup>

Does Chinese investment come with implicit strings attached and can it act as a Trojan Horse affecting European norms and policies, from human rights to labor laws? It is too early to tell, but investment could potentially translate into policy change, both at the domestic and foreign policy levels.

### 1. Implications on foreign policy

Even if conditionality is implicit, the competition between EU member states to host Chinese FDI could lead to a reversal of policy positions concerning Tibet, human rights in China, and Taiwan, for instance. It could also lead to stronger EU support for lifting the arms embargo against China.

On the issues of granting "market economy status" to China in the WTO and the place of China in the IMF, notably on voting rights, the conditionality has been made more than implicit. In September 2011, Premier Wen argued that the EU should grant China market economy status in exchange for continued purchase of member state sovereign debt – presumably the argument could also apply for continued influx of FDI into European countries. Indeed, Iceland was, in April 2012, the first European (though non EU) country to recognize China's market economy status at the same time as the launching of negotiations for a bilateral free trade agreement and promises of Chinese investment into Iceland.

### 2. Implications on domestic policy

Chinese FDI could also have an impact on domestic policies in EU countries. Competition between member states to attract investment could result in a regulatory race to the bottom, for instance when it comes to fiscal advantages or labor policies.

One problem with respect to labor is that Chinese companies investing abroad, especially construction companies, have a tendency to bring their own labor with them, which not only does not create jobs in the host country but also can give rise to domestic and even potentially racial tensions. This was the case for instance with the construction of the A2 highway between Warsaw and Lodz in Poland by the Chinese company Covec which tried to bring workers from China instead of hiring locals, resulting in immigration violations and strong local resentment.<sup>19</sup>

But the biggest implication on labor policy is most likely the softening of labor standards in the host country, which may turn a blind eye to labor violations in order to court and keep the Chinese investment. The example of the Chinese management of the main pier in the

---

<sup>18</sup> (Lim, 2011)

<sup>19</sup> (Millner, 2012)

port of the Piraeus in Athens should be watched closely. One condition put forth by the Chinese port operator COSCO was that none of the more than 500 workers be unionized. Numerous abuses of working conditions have been reported, such as 8-hour shifts with no meal or bathroom breaks, workers having to be available 24/7, no overtime pay for working night or weekend shifts, and salaries half of what they are at the neighboring Greek-operated pier.<sup>20</sup>

The fear exists that these initial Chinese investments represent a beachhead from which China will spread its own labor model into Europe and that companies which are run by Chinese masters will inevitably influence those that are not. As the president of the dockworkers union at the Piraeus declared, *"the result is that companies not run by the Chinese are being influenced by what the Chinese are doing in lowering the labor costs and reducing workers' rights."*<sup>21</sup>

Other instances of Chinese labor conditionality have been reported, such as recent rumors about a massive Chinese investment in future EU member state Croatia that would be accompanied by 20,000 Chinese workers.<sup>22</sup>

The recent declaration of the chairman of the China Investment Corporation Jin Liqun about European labor practices suggests that this might become a major political issue in the future: *"I think the labour laws are outdated. The labour laws induce sloth, indolence, rather than hardworking. The incentive system is totally out of whack. Why should, for instance, within [the] eurozone some member's people have to work to 65, even longer, whereas in some other countries they are happily retiring at 55, languishing on the beach? This is unfair."*<sup>23</sup>

#### **IV. IMPACT OF CHINESE OFDI ON EUROPEAN INSTITUTIONAL PROCESSES**

In addition to changes in foreign and domestic policies, Chinese investment in Europe could also potentially affect European institutional processes. The U.S. possesses robust formal procedures for vetting foreign investments, which have been designed and refined in the wake of successive crises provoked by specific instances of FDI, from the initial creation of the Committee on Foreign Investment in the United States in 1975, following fears generated by investment from the Gulf states, to the Exon-Florio amendment passed in 1988 in the midst of fears about Japanese investment, through to the 2007 Foreign Investment and National Security Act (FINSIA) enacted in reaction to the Dubai Ports controversy. In the EU, by contrast, no commonly agreed procedures exist for dealing with

---

<sup>20</sup> (Lim, 2011)

<sup>21</sup> (Lim, 2011)

<sup>22</sup> (Croatian Times, 2012)

<sup>23</sup> (Liqun, 2011)

foreign investment. Yet there is a real potential for Chinese FDI to impact the process of European integration, either positively or negatively.

### 1. Centrifugal pressures

Europe is stronger when it is united. The current competition between the member states, with its potential to lead to a regulatory “race to the bottom”, not only does not enable the EU to realize its potential but can also weaken the EU. The influx of Chinese FDI suggests the need for a coordinated response and should prompt a serious reflection about creating a “single voice” in investment as already exists in trade. The pressures from Chinese investment can have a centrifugal effect on European integration, reinforcing a development already enshrined in the Lisbon Treaty, which brought foreign investment under exclusive EU competence, per articles 206 and 207.

For the moment, national legal regimes vary considerably and each member state deals with foreign investment independently, with its own national rules and obligations, including those deriving from the twenty-six Bilateral Investment Treaties with China<sup>24</sup>. Some member states (e.g. France) have rules for vetting investment which are more constraining than others (e.g. Hungary). Yet when it comes to national security, an investor could be turned down by one member state and try its luck in another one instead, with the result that the national security of the first one would be compromised anyway.

One avenue of response is the establishment of an EU-wide body to vet foreign investments, à la CFIUS. Of course it could not be a functional equivalent to CFIUS which reviews investments based on national (or EU-wide) security considerations. It could include sectors that need special protection or sensitive sectors for defense and security. Another (alternative or complementary) avenue is to strengthen the monitoring of foreign investment on grounds of competition policy, which applies particularly to the case of China, given the great number of investment deals proposed by state-owned companies. Both responses would reinforce the “actorness” of the EU in global economic policy.

### 2. Centripetal pressures

Yet the influx of Chinese FDI can also have a reverse effect, exerting centripetal pressures on European integration.

#### a. “Divide and rule”

Chinese companies have so far exploited the high level of fragmentation and lack of coordination within the EU to obtain the best conditions, thanks to the competition that member states are waging against each other with all kinds of policy incentives to attract Chinese investment. This was particularly evident in the Poland-Central Europe-China trade and investment summit in April 2012, where Central and Eastern European countries

---

<sup>24</sup> Ireland does not have a BIT with China.

and companies were competing to attract Chinese capital and business. In so doing, they have started to create a pro-China lobby, which will make it more difficult for member states to agree to common rules for overseeing foreign investment, which China may find constraining. States with high levels of Chinese FDI, or hoping to attract high levels, will not argue in favor of a supranational investment regime that might restrict certain investments. This is a typical “divide and rule” strategy.

b. Fear of reciprocity

Another centripetal force is the fear of reciprocity, both in trade and investment, especially in an already tense political context of greater international pressure on China to accelerate its efforts to open up to foreign businesses and avoid distorting practices. For export-oriented countries like Germany, the worry is great that a supranational regime that reviews and constrains investments will trigger restrictions on imports from Europe. Staying open for Chinese investors is essential to prevent protectionist reactions in China. Another fear of reciprocity comes from member states which are themselves big investors abroad, such as France. Their large companies worry that a EU-wide regime will prompt more restrictions on their own foreign investments in China, especially in China which is gradually liberalizing its own domestic market to foreign investors per the December 2011 “Foreign Investment Industrial Guidance Catalogue”<sup>25</sup> and recent indications that it may soon raise the investment quota for foreign companies.<sup>26</sup>

c. A misleading signal

Finally, all member states, as well as European institutions, are afraid that the creation of a supranational procedure or body for reviewing foreign investment will send a misleading signal to China and other investors that the EU is stepping back from its commitment to an open investment regime. The centripetal forces seem stronger than the centrifugal forces at this point.

## V. IMPACT OF CHINESE OFDI ON THE TRANSATLANTIC RELATIONSHIP

While the influx of Chinese investments can have a divisive effect within the EU, will it also have a divisive effect on the transatlantic relationship or, on the contrary, will it lead to more cooperation as the EU and the U.S. increasingly find themselves “in the same boat” in the new world of globalization?

1. Potential for different European and American trajectories

As China seeks to diversify its assets, both the U.S. and the EU are attractive destinations for investment, but very recent trends point to a faster growth of Chinese FDI in the EU than in

---

<sup>25</sup> (Hanemann, 2012)

<sup>26</sup> (Reuters, 2012)

the U.S. Europe became the first destination for Chinese OFDI in 2011, while the momentum slowed at the same time in the U.S. Indeed, Chinese investments had settled into a roughly equivalent distribution between European and American projects from the start of the “going out” policy on, but the trajectories sharply diverged in 2011, which saw \$4.5 billion Chinese FDI in the U.S. and a record high of almost \$10 billion in the EU, a threefold increase from about \$3 billion in 2010.<sup>27</sup>

## 2. Potential for competition

The EU is the U.S.’s most formidable competitor and readily available substitute when it comes to Chinese OFDI, for greenfield projects as for acquisitions, because they can both provide Chinese investors with brands, know-how, technology, qualified labor, and distribution channels to consumers. The diverging transatlantic trajectory observed in 2011 could prompt Europeans to exploit an apparent comparative advantage.

Chinese government and corporate officials perceive, rightly or wrongly, that the U.S. is an inhospitable environment for Chinese investment, based largely on the widely publicized failure of the CNOOC takeover of UNOCAL in 2005 and, more recently, the two failed investments by Huawei in 3Com and 3 Leaf. The CFIUS process is interpreted as lacking transparency and predictability and as discriminating against Chinese investors –a perception which stems partly from the mandatory requirement to review deals involving state-owned enterprises. This is compounded by an American electoral climate in which China is being scapegoated and fingerpointed.

EU member states can capitalize on this perception and exploit the lack of restrictive investment controls and the inexistence of an EU investment review process in order to siphon potential investment away from the U.S. EU member states are engaged in aggressive investment promotion efforts, which often insist on the ease with which investments are approved, such as the April 2012 Poland-Central Europe-China forum.

Recent European efforts to start negotiations on a EU-China Bilateral Investment Treaty (BIT) could also drive a wedge between Europe and the U.S. Such a treaty would help European investors gain larger market shares in China while facilitating mergers and acquisitions by Chinese multinationals in Europe. Meanwhile, similar talks of launching a U.S.-China BIT have been stalled since 2009, and despite frequent American studies of the benefits of such a treaty and multiple announcements that this was in the works, no progress has been made on the other side of the Atlantic. If China engages into negotiating a bilateral investment framework with the EU but not the U.S., let alone signs a treaty with one but not the other, this would probably increase further the divergence in Chinese FDI trajectories in Europe and the U.S. and lead to some damaging consequences on the transatlantic partnership.

## 3. Potential for cooperation

---

<sup>27</sup> (Hanemann, 2012)

This economic competition can also have serious ramifications for U.S. national security and, therefore, prompt strong demands for transatlantic cooperation from the Americans.

By bypassing the American vetting of investment for national security concerns, Chinese firms can get access to potentially threatening technology from Europe and acquire firms that develop technology for the U.S. military. For example, in fall 2010, an Italian fiber optic cable manufacturer finalized a deal to purchase a Dutch rival, Draka Holding NV. The U.S. Navy and several other Western militaries use Draka's products for secure communications. One week after the deal was finalized, a Chinese investment corporation put in a counter offer 30% higher than the Italian one, totaling \$1.3 billion. It is widely suspected that the Chinese government secretly backed the investment corporation's counteroffer.<sup>28</sup> As for Huawei, which has faced many roadblocks in the U.S., it continues to massively expand its presence in Europe.

The opportunities and dangers posed by the influx of Chinese OFDI could also press the EU and the U.S. for more regulatory cooperation. Many of the challenges represented by Chinese investment, from the state-owned nature of the investors to the absence of level-playing field for Western investors in China, are better addressed in a cooperative fashion which could be tackled by the OECD, for instance. Indeed, the EU and the U.S., each other's largest recipient and source of FDI, agreed in April 2012 on a Statement of Shared Principles for International investment, which shows a growing commitment to cooperation, not competition.<sup>29</sup>

## CONCLUSION

Respected magazines all over Europe have used on their cover pages menacing images of fiery dragons spewing banknotes or contemporary Maos with imperialistic designs on the continent. These images cohabit with pictures of smiling European heads of state shaking hands with Chinese officials. This contrast illustrates the challenge posed by the surge of Chinese investment into Europe: how to ensure the benefits from FDI, from job creation to productivity gains, while protecting from its harmful effects.

European publics are for the moment ambiguous towards this unprecedented situation. Opinion polls show that Europeans are split when it comes to viewing China as an opportunity or a threat. Of individuals in the twelve EU countries surveyed in the 2011 edition of the Transatlantic Trends poll, 41% see the Chinese economy as a threat while 46% see it as an opportunity. This reflects vast differences among countries, the French at

---

<sup>28</sup> John W. Miller, "Chinese Companies Embark on Shopping Spree in Europe," *The Wall Street Journal*, June 6, 2011, <http://online.wsj.com/article/SB10001424052748704355304576214683640225122.html>.

<sup>29</sup> (Bierbrauer, 2012)

one end of the spectrum with 56% seeing China as a threat, the Dutch on the other end with only 22% interpreting China as a threat.<sup>30</sup>

In the end, even though hosting Chinese OFDI in Europe is not free from risk, the benefits outweigh the costs. First, OFDI provides an influx of capital into the struggling economies, increasing employment at no cost to the taxpayer. Second, jobs in foreign affiliates are typically better remunerated than similar jobs in domestically owned companies. Third, keeping the EU open to foreign investment demonstrates a global example for international openness. Finally, Chinese money refused by the EU could alternatively be directed to competitors or even enemies.

In order to welcome Chinese OFDI in Europe while dealing with its potential dangers, the EU needs to offer a coordinated response, both between member states and with the U.S. Policy recommendations include: craft a supranational procedure for reviewing investments that is apolitical, non-discriminatory, predictable, and provides confidence and trust; regulate the incentives and “race to the bottom” competition waged by EU member states to attract FDI; conclude a BIT with China; and encourage Chinese firms to showcase their investments’ contributions to European societies, such as engaging in philanthropic activities in local communities, in order to stem any xenophobic reflex.

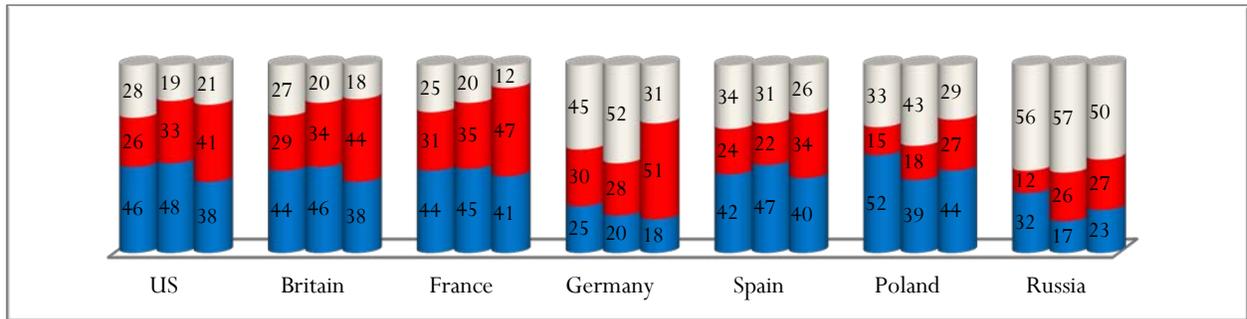
Chinese investors find themselves at the right place at the right time. The predicted surge of Chinese investment in Europe presents great opportunities; after all, it is better for the EU if Chinese companies come to Europe and employ local workers than if European companies go East to employ Chinese workers. But in order for this investment to truly rescue European economies, Europeans have to be careful to present a unified response so that China does not end up ruling by dividing, carving out concessions in the heart of Europe as an irony of history.

---

<sup>30</sup> (German Marshall Fund, 2011)

## Annex

### Annex 1: Who is the leading economic power in the world today?



Source (Pew Global Attitudes Project, 2011)

## Annex 2

### List of recent proposed and actual Chinese FDI deals in the EU

January 2012	Shandong Heavy Industry Group-Wenchai	Ferretti yachts (A)	Italy
Announced January 2012	Liu Gong	HSW bulldozers (A)	Poland
January 2012	Sany Heavy Industry	Putzmeister (A)	Germany
February 2012	Great Wall Motors	Automotive plant (G)	Bulgaria
February 2012	LiuGong Machinery	Huta Stola Wola Road machinery maker (A)	Poland
March 2012	Linyung Industrial Group	Kiekert AG (A)	Germany
Announced April 2012	Chinese government?	Bozhurishte Industrial Zone (industrial and logistics park) (G)	Bulgaria
Announced April 2012	Chinese built rail line to Budapest airport		Hungary
Announced April 2012	Far Eastern Phoenix	Old Larnaca Airport	Cyprus
Announced May 2012	Bright Foods	Weetabix (A)	Great Britain

(A): acquisition

(G): greenfield



## LIST OF ACRONYMS

BIT	Bilateral Investment Treaty
CFIUS	Committee on Foreign Investment in the United States
CIC	China Investment Corporation
FDI	Foreign Direct Investment
FINSA	Foreign Investment and National Security Act
M&A	Mergers and Acquisitions
OECD	Organisation for Economic Cooperation and Development
WTO	World Trade Organization

## BIBLIOGRAPHY

---

- A Capital, 2012. *A Capital Dragon Index*. [Online]  
Available at: <http://www.acapital.hk/milestones.php>
- Barboza, D., 2011. As China Invests, U.S. Could Lose. *New York Times*, 4 May.
- Bierbrauer, E., 2012. *The EU and U.S. agree on open, transparent and non-discriminatory investment principles*, s.l.: European Parliament Directorate General for External Policies.
- Central and Eastern Europe Development Institute, 2012. *Partners or Rivals? Chinese Investment in Central and Eastern Europe*, s.l.: s.n.
- Croatian Times, 2012. PM says Chinese investments, hiring to be done by rules. *Croatian Times*, 30 April.
- Geitner, P., 2012. China, Amid Uncertainty at Home and in Europe, Looks to Germany. *The New York Times*, 22 April.
- German Marshall Fund, 2011. *Transatlantic Trends*, s.l.: s.n.
- Godement, F. & Parello-Plesner, J., 2011. *The Scramble for Europe*, London: European Council on Foreign Relations.
- Hanemann, T., 2012. *Building a Global Portfolio: What China Owns Abroad*. [Online]  
Available at: <http://rhgroup.net/notes/building-a-global-portfolio-what-china-owns-abroad>
- Hanemann, T., 2012. *Chinese FDI in the United States: Q4 2011 Update*, s.l.: The Rhodium Group.
- Lauter, D., 2011. French fear being indebted to China. *Los Angeles Times*, 26 November.
- Lim, L., 2011. In Greek Port, Storm Brews over Chinese-Run Labor. *NPR Morning Edition*, 8 June.
- Liqun, J., 2011. *Europe induces 'sloth, indolence'*, s.l.: Al Jazeera.
- Millner, C., 2012. Beijing sets its sights on Central Europe. *Der Spiegel*, 18 May.
- Organization for Economic Cooperation and Development, 2008. *OECD Benchmark for Foreign Direct Investment-Fourth Edition*, s.l.: s.n.
- Pew Global Attitudes Project, 2011. China Seen Overtaking US as Global Superpower. 13 July.
- Qingfen, D., 2012. China's Outbound Investment Rises in Q1. *China Daily*, 17 April.
- Reuters, 2012. China may raise investment quota for foreigners: paper. 15 May.
- Rosen, D. & Hanemann, T., 2011. *An American Open Door? Maximizing the Benefits of Chinese Foreign Direct Investment*, s.l.: Asia Society.
- The Economist, 2010. China buys up the world. *The Economist*, 11 November.
- Xu, T., Petersen, T. & Wang, T., 2012. *Cash in Hand: Chinese Foreign Direct Investment in the U.S. and Germany*, s.l.: Bertelsmann.

