

Last working version before publication in Julien Chaisse ed., [CHINA'S THREE-PRONG INVESTMENT STRATEGY: BILATERAL, REGIONAL, AND GLOBAL TRACKS](#) (London: Oxford University Press, February 2019)

BEWARE OF CHINESE BEARING GIFTS: Why China's Direct Investment Poses Political Challenges in Europe and the United States

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From a non-existent player fifteen years ago, China has now become one of the largest senders of Foreign Direct Investment (FDI) flows in the world. By and large, this new provenance of capital has been welcomed by host countries, especially given the drop in other sources of FDI in the wake of the American financial crisis in the late 2000s. This new investment has created jobs locally, it has enabled to keep some troubled firms afloat, and it has often opened up the Chinese market for local companies. FDI is indeed the backbone of economic globalization and a crucial source of transmission of capital, technology, and people across borders.

The exponential growth of Chinese direct investment, however, has also been accompanied in some cases by controversy and even resistance, both in developing and in developed economies. Around the world, critics have expressed fears and denounced some of the potential dangers of this investment, such as lowering of local labor standards, hollowing out of industrial core through repatriation of assets, and acquisition of dual use technology. Alarmist media headlines have warned against a Chinese takeover of national economies one controversial investment deal at a time. The ensuing political backlash has often received considerable media attention and increased scrutiny over subsequent deals.

What explains the political challenges posed by the recent explosion of Chinese direct investment in the United States (U.S.) and the European Union (EU)? How and why have attitudes and policies in the West changed over the past decade towards Chinese FDI? This chapter considers two alternative explanations for the political challenges triggered by Chinese investment in Western countries. The first is that Chinese FDI causes political unease because of its novelty. The second is the perception that there is something inherently different about the nature of Chinese FDI and therefore it should not be treated politically like any other foreign investment. These two explanations lead to a different set of predictions for the future of Chinese FDI in Europe and the U.S.

The first section analyzes how the novelty of Chinese FDI may pose political challenges to Western politicians and publics and compares the current phenomenon with past instances of politically problematic sources of FDI. Section Two examines the argument that there is something inherently different about Chinese FDI, notably as stemming from an emerging economy, a unique political system, and a non-ally in the security dimension. The third section explores the domestic political context in which these challenges are raised: in Europe, the euro crisis and the rise of populism; in the U.S., the focus on geopolitical competition and the rise of economic nationalism. The conclusion raises some implications of these political challenges on the future of Chinese outward investment.

I. THE NOVELTY OF CHINESE FDI AS POLITICAL CHALLENGE

From CNOOC's lease of the Greek port of Piraeus and Geely's acquisition of Swedish automaker Volvo to Dalian Wanda's purchase of AMC Cinemas, Fosun's takeover of hotel chain ClubMed and Suning's investment in the InterMilan soccer club, foreign investment emanating from China has captured the attention of the European and American media. One explanation for this heightened public attention on instances of Chinese direct investment comes from its novelty. This section explores the novel phenomenon of Chinese direct investment in Europe and the U.S., compares it with past instances of politically controversial sources of foreign investment, and analyzes the existence of a political threshold for FDI.

Chinese direct investment, a novel phenomenon

Chinese investment in Europe and the U.S. barely existed a mere decade ago. This novelty has proven by itself a source of anxiety; initially people did not know what to make of this new phenomenon and expressed worries. This perception of a new source of investment as something to be feared is consistent with a long-held finding in the management literature on FDI about the "liability of foreignness"¹ and the "costs of doing business abroad".² New and foreign is challenging, at least temporarily, especially if the institutional and cultural distance between host and home country is large.

It is not only the novelty but also the rapidity of the expansion that proved cause of alarm. Indeed, Chinese investment in Western economies has risen almost exponentially over the past

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Acknowledgments: Many thanks to Julien Chaisse and the participants to the Asia FDI Forum II at the Chinese University of Hong Kong Graduate Law Center, 29-30 November 2016.

¹ Srilata Zaheer, 'Overcoming the Liability of Foreignness' (1995) 38 *Academy of Management Journal* 341–63, doi:10.2307/256683; Lorraine Eden and Stewart R Miller, 'Distance Matters: Liability of Foreignness, Institutional Distance and Ownership Strategy' in *Theories of the Multinational Enterprise: Diversity, Complexity and Relevance, Advances in International Management* (Emerald Group Publishing Limited, 2004) 187–221, doi:10.1016/S0747-7929(04)16010-1.

² Steven Hymer, *The International Operations of National Firms* (Lexington, MA: Lexington Books, 1976) 1.

decade: from virtually non-existent in 2005, China is now one of the top three home countries for FDI in the world in flows. In the United States, the stock of Chinese investment grew from almost zero in 2005 to close to \$150 billion by the end of 2016.³ In the European Union, the stock of Chinese investment had reached 50 billion euros by late 2015. Even more so than stock, flows contributed to shaping the impression of momentum, and therefore danger. Over half of all Chinese FDI flows in Europe and the U.S. since 2000 have taken place in the past three years.⁴ Chinese FDI rose 50% between 2015 and 2016 and has doubled since 2012.⁵ In the U.S., Chinese FDI flows surpassed \$50 billion in 2016. They tripled between 2015 and 2016.⁶ In the EU, FDI from China rose 90% in the past year.⁷ In Germany, FDI deals from China were multiplied by 10 from \$1.3 billion in 2015 to \$12.1 billion in 2016.⁸

Moreover, it is not only the novelty but also the ubiquity of the expansion that fuels worries. China is investing everywhere in the world: Europe and the U.S. are the latest destinations in a long list that started with resource-rich African countries and now includes the majority of countries in the world, from Australia to Canada by way of Central Asia. Chinese investment is also ubiquitous in every economic sector, including information technology, infrastructure, food products, tourism, industrial machinery, financial services, entertainment, and real estate.⁹

An additional source of worries has been the coupling of the novelty of Chinese direct investment with its rapidly expanding relative weight compared to other sources of FDI. Chinese investment was rising everywhere in absolute terms but it was also rising in relative terms. Indeed, the take-off of Chinese direct investment in Europe and the U.S. coincided with the sharp decline of FDI worldwide until 2012 in the wake of the U.S. financial crisis, especially in the EU. This relative growth has amplified the new phenomenon of Chinese investment to the public and made it seem scarier.

Finally, the nature of the investment deals initially made by Chinese companies increased the public spotlight. In general, greenfield investment is seen as more innocuous and less politically problematic than mergers and acquisitions. Yet the vast majority of Chinese investment in Europe and the U.S. , at least in the early years, were takeovers. In 2016, acquisitions drove 97% of the

³ Derek Scissors, 'Record Chinese Outward Investment in 2016: Don't Overreact,' *AEI* (2017) 1, available at <www.aei.org/publication/record-chinese-outward-investment-in-2016-dont-overreact/>.

⁴ Baker McKenzie, 'Chinese Investment Tripled in US in 2016, Doubled in Europe,' (2017) 1, available at <www.bakermckenzie.com/en/newsroom/2017/02/chinafdi>.

⁵ Derek Scissors, 'Record Chinese Outward Investment in 2016: Don't Overreact,' *AEI* (2017) 1, available at <www.aei.org/publication/record-chinese-outward-investment-in-2016-dont-overreact/>.

⁶ Baker McKenzie, 'Chinese Investment Tripled in US in 2016, Doubled in Europe,' (2017) 1, available at <www.bakermckenzie.com/en/newsroom/2017/02/chinafdi>.

⁷ Baker McKenzie, 'Chinese Investment Tripled in US in 2016, Doubled in Europe,' (2017) 1, available at <www.bakermckenzie.com/en/newsroom/2017/02/chinafdi>.

⁸ Baker McKenzie, 'Chinese Investment Tripled in US in 2016, Doubled in Europe,' (2017) 1, available at <www.bakermckenzie.com/en/newsroom/2017/02/chinafdi>.

⁹ Baker McKenzie, 'Chinese Investment Tripled in US in 2016, Doubled in Europe,' (2017) 1, available at <www.bakermckenzie.com/en/newsroom/2017/02/chinafdi>

value of FDI activity in Europe and the U.S.¹⁰ These are more likely to touch off opposition, no matter what the origin of the investment is.

Past instances of political challenges posed by novel sources of FDI

Chinese FDI startled the media and politicians at the beginning because it was a new phenomenon. It is not the first time, however, that foreign investment poses political challenges in the host country. This section explores briefly two prior instances of political controversy raised by foreign investment in Europe and the United States.

In Europe, one precedent is the ‘coca-colonization’ by American multinationals that occurred from the 1960s onwards. Massive investment by U.S. companies created existential frictions in countries where the imported production processes and type of goods produced seemed to threaten the traditional way-of-life.¹¹ Nowhere was this fear more pronounced than in France, which resisted loudly this “American challenge”, as coined in a 1968 bestselling book.¹² A later mobilization occurred with a new wave of American investment in France in the 1990s, which included the creation of the Disneyland Paris amusement park and a push by American fast food companies into France.¹³ This second wave of hostility towards American FDI culminated with the opposition to the Multilateral Agreement on Investment (MAI) negotiated under the auspices of the OECD, which ultimately failed in 1998 after France withdrew its support.¹⁴ Since then, opposition to American investment has become mostly muted, even though the United States is still one of the top sources of inward FDI flows and stocks in France.

Another instance of political controversy raised by foreign investment in the host country happened in the late 1980s, which saw an explosion of Japanese FDI into the United States. American media and politicians became obsessed with the “Japanese invasion” when acquisitions and greenfield investments from Japan experienced a rapid influx from less than \$1 billion of annual inflows in 1980 to \$18 billion by 1990.¹⁵ A collective sense of panic swept the country as Japanese investors went for high-profile deals, such as the 1989 acquisition of New York City’s Rockefeller Center by the Mitsubishi Group and of Columbia Pictures by Sony, fueling perceptions that Japan was taking over the U.S.

The fears raised by this Japanese investment “invasion” prompted policy change to restrict the openness of the U.S. to foreign investment. The proposed takeover in 1988 of the semiconductor firm Fairchild by the Japanese Fujitsu Ltd provoked intense backlash. This particular deal prompted Congressional action, which resulted in 1988 in the Exon-Florio

¹⁰ Baker McKenzie, 'Chinese Investment Tripled in US in 2016, Doubled in Europe,' (2017) 1, available at <www.bakermckenzie.com/en/newsroom/2017/02/chinafdi>

¹¹ Richard F. Kuisel, *Seducing the French: The Dilemma of Americanization* (University of California Press, 1997) 1.

¹² Jean-Jacques Servan-Schreiber, *The American Challenge* (Avon Books, 1968) 1.

¹³ Richard F. Kuisel, *The French Way: How France Embraced and Rejected American Values and Power* (Princeton University Press, 2011) 1.

¹⁴ Stephen J. Kobrin, 'The MAI and the Clash of Globalizations,' *Foreign Policy* (1998) 97–109.

¹⁵ Curtis Milhaupt, 'Is the U.S. Ready for FDI from China? Lessons from Japan’s Experience in the 1980s,' in Karl Sauvart, *Investing in the U.S.* (2008) 1.

amendment (50 U.S.C App. § 2170) authorizing the president to “investigate foreign acquisitions, mergers, and takeovers of, or investments in, U.S. companies from a national security perspective”. President Reagan in turn delegated this authority to CFIUS. Further restrictions were added by the Byrd Amendment of 1992 (Section 837(a) of P.L. 102-484), which required CFIUS to investigate proposed foreign investments when the acquirer is acting on behalf of a foreign government, and by the 2007 Foreign Investment and Security Act (FISIA) (P.L. 110-49), which expanded CFIUS’ mandate to include a broader range of national security risks.

A FDI novelty curve?

Both historical examples suggest that foreign investments that provoked passionate opposition in the past have continued on without notice once they became normalized in the host country. In both cases, the more investment took place, the more the fears went away and the nationality of the investor became a non-issue. Novelty eventually wears off.

The controversies provoked by Japanese investment in the U.S. in the 1980s provide probably the closest historical precedent to the current situation with Chinese investment. The context was eerily similar, marked by trade deficit, currency disputes, arguments over state subsidies and, above all, the rapid rise in relative power of an Asian country in an age presented as that of American decline.

This historical example may suggest the existence of a “FDI novelty curve”: the initial investments were met with no particular reaction at first. As more investments started pouring in, media and politicians started to put the spotlight on this new phenomenon and the fears snowballed into new legislation. Once a certain threshold of Japanese investments that continued to contribute positively to the American economy was met, interest in the issue plummeted. This was due to several reasons.

First, the economic effects of Japanese investment on the American domestic economy seemed overall positive. It contributed directly to the preservation and the creation of jobs, especially high-wage jobs, and R&D spillovers flowed into the local economy. Second, the liability of foreignness seems to disappear with time. American people got used to what appeared so foreign at the outset, namely, Japanese owners and managers. Third, the fears raised by critics of Japanese investment plainly failed to materialize. As a result, today Japan is the second largest source of FDI in the United States.

These two examples of American investment in France and Japanese investment in the U.S. suggest, as historical precedents, that the growing familiarity with Chinese companies and potential of Chinese FDI to become a source of economic vitality in the host country will, over time, replace the initial worries raised by the new phenomenon. If novelty is indeed the explanation for the political challenges currently raised by FDI from China in Europe and the U.S., then these political concerns should decline as Chinese investment projects accumulate and become normalized in a few years.

II. THE DISTINCTIVENESS OF CHINESE FDI AS POLITICAL CHALLENGE

By contrast, a second explanation for the political anxiety triggered by Chinese direct investment in Europe and the U.S. is based on the argument that there is something inherently different and unique about Chinese FDI. It is not a matter of novelty but one of the intrinsic characteristics of FDI from China. This section explores how the case could be made for uniqueness on at least three counts –emerging economy, unique political system, and security non-ally.

An emerging economy

In spite of its spectacular growth over the past few decades, China is still, by all measures, an emerging economy. This characteristic poses its own set of political challenges when the United States and European countries host FDI from China.

First, the influx of direct investment from a developing to a developed economy, which has no historical precedent, shakes the traditional political dynamics of FDI and poses somewhat of an existential problem for the host countries. They are more accustomed to investing in emerging, problematic economies than to being treated like one of them.¹⁶ Historically, direct investment has flowed almost exclusively from developed to developing economies. Capital was a source and symbol of power. FDI was criticized in the host countries for being an instrument of neo-imperialist dependency.¹⁷ Chinese investment into Europe and the U.S. can be interpreted as an external sign that the tables have turned and as a precursor of what might be yet to come –a gradual slide of Western power relative to the rising power of China. As such a symbol, it is expected that some politicians and population in the host countries will put up a fight and resist what they see as evidence that the tables are turning.

Second, the usual benefits for the host economy that accompany inward foreign investment may not happen in a case where the investor is from a less advanced economy than the target of the investment. FDI always has costs and benefits for the host country, but typically the benefits outweigh the costs, notably through technological and know-how spillover. FDI fuels technological progress, a major driver of economic growth, because foreign firms usually bring with them superior management strategies and technologies developed in their home countries, as was the case of Japanese automobile producers in the U.S. or American computer companies in Europe. These spill over into the local economy as workers and R&D move from the foreign-owned to national firms.

In the case of Chinese investment, however, some fear that the net positive economic impact may not happen because the technological and know-how flows do not appear to be going in the

¹⁶ Sophie Meunier and others, 'The Politics of Hosting Chinese Investment in Europe' (2014) 12 *Asia Europe Journal* 109–26.

¹⁷ Immanuel Wallerstein, 'The Rise and Future Demise of the World Capitalist System: Concepts for Comparative Analysis' (1974) 16 *Comparative Studies in Society and History* 387–415; Robert Gilpin and Jean Gilpin, *The Political Economy of International Relations* (Princeton, NJ: Princeton University Press, 1987) 1; Dani Rodrik, *Has Globalization Gone Too Far?* (Washington, DC: Institute for International Economics, 1997) 1.

‘traditional’ direction, from the home to the host country. With the exception of a few sectors, such as telecom equipment and port management, Chinese investors seem to be looking to invest precisely in Western firms whose main assets are their superior technology and know-how, from robot makers in the German Mittelstand to Hollywood production and distribution companies. An Italian analyst has called this the “reverse Marco Polo effect”:¹⁸ this time it is the Chinese who are going to Europe to acquire technological innovation. This phenomenon is not limited to high-technology fields. It is also at play, for instance, in European football, where the fast-paced acquisition of foreign companies and players is seen as a fact-finding exercise in order to jumpstart Chinese soccer know-how and turn China into a “soccer powerhouse”, in the words of President Xi Jinping.¹⁹

Third, the differentials in technology and wages between the emerging economy investor and the developed economy host country may potentially lead to asset-stripping. In that case, the Chinese investor could repatriate to China the assets of the company it took over and virtually close up shop in the host country –some critics even talk of a “siphoning off”. The advantages for the investor are clear, such as legal acquisition of technology and know-how, as well as international cachet and reputation of brands which would manufacture everything in China. For the host country, in the short term such a scenario would bring only the costs of FDI, not the benefits, notably because the foreign investment would accelerate the loss of local employment. In the long term, the consequences could be even more damaging as the host country would see an erosion of its competitive lead.

A unique political system

A second feature making Chinese investment different from historical precedent is the uniqueness of China’s political system and of “capitalism with Chinese characteristics”, which potentially pose several political problems for the host country. The most important problematic feature is undoubtedly the central role of the Chinese state in the economy. American and European democracies have little experience in what it means to have a foreign state manage (or not) companies’ investment decisions, thereby fuelling several political concerns about the potential negative implications of the role of the Chinese state for host countries.

For one, the injunction to Chinese firms to “go out” has been the official policy of the Chinese government in successive five-year plans since 2000 for a variety of reasons, including the need to diversify the placement of foreign reserves, acquire resources and technologies, ease its access to foreign consumer markets, and further its international ambitions. For over a decade, Chinese firms and their managers received a series of carrots and sticks to internationalize their operations, such as financial incentives and individual career advancement. This “going out” policy has been reinforced with the launch of the One Belt, One Road (OBOR) initiative in 2013 aiming to connect the Chinese economy with countries along the ancient silk and maritime roads,

¹⁸ Rebecca Valli, ‘Italian Entrepreneurs Turn to Chinese for Help’ *VOA* (2012) 1, available at <www.voanews.com/a/italian-entrepreneurs-turn-to-chinese-for-help/1507976.html>.

¹⁹ Owen Gibson, ‘The Great Windfall of China: A Football Revolution That May Lead to World Cup’ *The Guardian* (2016) 1, available at <www.theguardian.com/football/blog/2016/feb/06/china-football-revolution-world-cup>.

crossing Central Asia all the way to Western Europe. Therefore it is rational for host countries to interpret Chinese FDI as being directed centrally by China's government.

Moreover, the nature of the relations between Chinese investors and the Chinese government is often confusing. A majority of Chinese direct investment abroad is conducted by State Owned Enterprises (SOE) – though the proportion is smaller in Europe and especially in the U.S. than in the rest of the world. Even in the case of transactions conducted by private investors, doubt persists as to the actual influence of the Chinese government and Communist Party. This has been an issue, for instance, with efforts to invest in the U.S. by Huawei, a private company, whose owner is rumored to entertain very close links with the Chinese government. Moreover, the lack of transparency of the governance structure of Chinese firms, whether state-owned or private, makes the investment transaction difficult to comprehend for the target company or the host country. In some cases, the deal by a Chinese company seems to have been spearheaded by someone who was either mysterious or not the actual person in charge – a public example of this happened in the case of the acquisition of a stake in the Toulouse-Blagnac airport in France by a Chinese investment consortium headed by Mike Poon, who later mysteriously disappeared.

The opaque involvement of the Chinese government in the decisions of its companies to invest abroad also leaves some lingering doubt as to the ultimate rationale for the investment. Is it purely a commercial decision responding to market incentives or is there an ulterior motive to the deal? American and European politicians do suspect in some cases that these companies are acting to fulfill strategic goals, rather than market-developing and profit-maximizing goals.

The Chinese political economy model of state-led capitalism also leads Chinese companies to assume a different attitude towards risk than do market-driven capitalist companies. The Chinese state conducts explicit industrial policy whereby national champions are identified and backed with abundant subsidies and administrative help. They have access to cheap credit. This enables these companies to take more risks and be less concerned about immediate return and bottom-line. They can plan for the long instead of the short term and, therefore, offer bids which are higher than those of their privately-owned competitors.

Finally, the political economy of Chinese investment leads to fears that the government can manipulate the transaction by using its special leverage. This fear was illustrated by the case of Aixtron, a German technology company specialized in semi-conductors. In 2015, Sanan Optoelectronics, a Chinese customer of Aixtron, canceled a large order at the last minute, which provoked a crash of the price of Aixtron's shares. A few months later, the Chinese investment fund Fujian Grand Chip made a deal to acquire Aixtron. According to the press, Sanan and Fujian had many connections, including a common investor, and were both linked to the Chinese government.²⁰

²⁰ Paul Mozur and Jack Ewing, 'Rush of Chinese Investment in Europe's High-Tech Firms Is Raising Eyebrows' *The New York Times* (2016) 1, available at <www.nytimes.com/2016/09/17/business/dealbook/china-germany-takeover-merger-technology.html>.

Not a security ally

A third feature pleading for the distinctiveness of the political challenges posed by Chinese FDI come from strategic security considerations. The United States and European countries are not used to receiving investment from countries which are not their security allies. The Soviet Union did not invest in the West during the Cold War. To be sure, China is not an enemy but rather a superpower with avowed geopolitical ambitions and foreign policy goals often at odds with those of the U.S. and some European countries. This raises several causes for concern about the ultimate motive of investment, including issues of dual-use technology and strategic leverage.

One concern relates to the efforts by Chinese investors to acquire technology abroad, which is problematic from a security standpoint for at least two reasons. First, even though China itself is not a security enemy, it is on friendly terms with some countries considered pariahs or rogue states in the West, such as North Korea. Some of the technology acquired through Chinese FDI in Europe and the U.S. could make its way in the hands of their leaders, with possible security implications.

Second, some Chinese investments that may seem innocuous at first glance may indeed have security implications. This could be, for instance, because of their strategic location, such as CASIL's investment in the Toulouse-Blagnac airport in France in 2015, which went through despite its location adjacent to the Airbus factory, and the Chinese-owned Ralls Corporation's investment in a wind farm in Oregon in 2012, which was blocked by presidential order because of its location overlooking a U.S. military base. It could also be because of the dangers of dual-use technology, with technology peacefully employed in everyday consumer products having the potential to be adapted for military use. Two recent examples of concerns about this potential can be found in the 2016 attempts by the Chinese group Go Scale Capital to acquire Lumileds, a subsidiary of the Dutch company Philips making lighting components, and by the Chinese company Fujian Grand Chip to acquire Aixtron, a German company manufacturing silicon chip equipment, both of which were blocked by a review in the Committee on Foreign Investment in the United States (CFIUS) because of their potential implications for American national security.

Another security concern relates to the risks of political leverage and control arising from foreign ownership and, therefore, dependence. One potential risk is physical leverage. For instance, the Chinese owner could strip the assets of the company acquired in the host country, for instance machinery or intellectual property, provoking lay-offs in the short term and removing competitive advantages in the longer run. Countries worry particularly about specific physical risks (e.g. sabotage, espionage, control) associated with foreign ownership of sensitive critical infrastructure, such as nuclear power plants. This was the crux of the decision by British Prime Minister Theresa May to reexamine and delay final approval of the Hinkley Point deal in 2016, on the grounds that China could build weaknesses on purpose into some of the nuclear safety systems or could shut down British electricity production at will, thereby unleashing chaos in the country.

Another potential risk, more subtle, is political leverage. China could potentially use its ownership of foreign assets to pressure and even coerce host governments into falling in line on the political issues that the Chinese government cares deeply about, such as the One-China Policy, the question of Tibet, and the issue of human rights.²¹ The higher the dependence of a foreign country on Chinese investment, the larger we could expect the implicit or explicit leverage of China on controlling that host country's public policy towards meeting with the Dalai Lama or denouncing Taiwan, for instance.

Divergences between European countries and the United States exist on all three main perceptions of the unique dangers posed by Chinese investment -emerging economy, unique political system, and security non-ally. These divergences are particularly pronounced with respect to national security issues, which are the main lens through which the U.S. has, up until now, been interpreting Chinese investment, whereas European countries have focused more on issues such as economic dependence and political leverage.

If the uniqueness of Chinese FDI, and not its novelty, is indeed the explanation for the political challenges encountered in Western democracies, then we should see political issues raised more in host countries as Chinese investment projects accumulate. This would manifest itself as increasingly negative articles in the media, changes towards more restrictive regulation and vetting of foreign investment, and an impact on negotiations of investment agreements.

III. THE DOMESTIC POLITICAL CONTEXT FOR HOSTING CHINESE FDI IN EUROPE AND THE U.S.

Whether the “novelty” or the “uniqueness” interpretation of the potential dangers posed by Chinese investment predominates depends in large part on the domestic political context in the host country. This section explores in turn the consequences for Chinese FDI of the evolving domestic political context in Europe and the United States.

Europe: The euro crisis vs. the rise of national populism

Two related features of European politics in recent years frame two different responses to Chinese investment: on one hand, the euro crisis has made Chinese investment more valuable and has fostered a public rhetoric presenting Chinese acquisitions as salvation; on the other hand, a growing national populism in European countries is turning increasingly negative towards globalization and towards “others”, including foreign investment.

The surge of Chinese investment in Europe coincided with the outbreak of the euro crisis for several reasons.²² For one, Chinese FDI started to arrive in Europe in the late 2000s as a result of

²¹ Sophie Meunier, 'A Faustian Bargain or Just a Good Bargain? Chinese Foreign Direct Investment and Politics in Europe' (2014) 12 *Asia Europe Journal* 143–58, doi:10.1007/s10308-014-0382-x.

²² Sophie Meunier, “Beggars Can’t Be Choosers”: The European Crisis and Chinese Direct Investment in the European Union' (2014) 36 *Journal of European Integration* 283–302.

official Chinese government injunctions to “go out” –European countries, as well as the United States, were last on the list of the destinations for Chinese investors because there were more political and regulatory hurdles and the type of investment targets in these host countries were more complicated to manage than the resource-seeking investments made by Chinese companies in Africa, for instance. The simultaneity of this surge of investment and the euro crisis was therefore partly coincidental –the timing set forth by the Chinese government happened to coincide with the crisis.

Chinese investment also surged in Europe precisely as a result of the euro crisis, which created opportunities for bargain deals. On one hand, the supply of European companies for sale increased because of bankruptcies and the bursting of property bubbles. With so many countries burdened by debt, many European public assets were also put up for sale as part of privatization programs. On the other hand, the demand for these assets dried up in Europe, where fewer local buyers were able to invest because of the crisis.

China was well-placed to take advantage of these bargains, first because it possessed a gigantic accumulation of foreign exchange reserves. Also, the American financial crisis had convinced Chinese leaders of the need to diversify, both away from the U.S. and away from sovereign debt. The SOE ownership of many Chinese investors enabled them to take higher risks, with the potential for higher returns.

As a result, Chinese investment was able to surge in Europe, both in the public and private sectors. For instance, in Portugal, Chinese investors acquired 45% of the total assets put for privatization under the Economic Adjustment Program and the IMF in sectors such as electrical infrastructure and financial services.²³ In Italy, Chinese companies invested in the power grid, deals that were made possible by a privatization program by former Prime Minister Matteo Renzi in order to reduce Italy’s national debt. In Greece, Chinese investors could take advantage of the many opportunities offered by the privatization program designed to meet the bailout conditions, including COSCO’s investment in the port of Piraeus in Athens.²⁴ In Germany, Chinese investors could acquire small and medium sized family companies that had been hurt by the global financial crisis, such as the Sany Group’s acquisition of concrete pumpmaker Putzmeister, whose revenue and staff had been cut by half since 2008 by the time of its takeover in 2012.²⁵

It should be noted, however, that many Chinese acquisitions in the wake of the euro crisis were not economic bargains per se. In several cases, these acquisitions were the result of public battles where Chinese investors outbid other interested parties by paying a hefty premium –such as was the case with Fosun’s acquisition of French resort chain ClubMed which happened in 2015 after an expensive, protracted two year takeover battle. Neither did Chinese investors jump at

²³ Anne-Claude Martin, 'Chinese Investments Soar in Crisis-Hit Europe' *EurActiv.com* (2014) 1, available at <www.euractiv.com/section/euro-finance/news/chinese-investments-soar-in-crisis-hit-europe/>.

²⁴ Sophie Meunier, 'A Tale of Two Ports: The Epic Story of Chinese Direct Investment in the Greek Port of Piraeus' *CritCom* (2015) 1, available at <<http://councilforeuropeanstudies.org/critcom/a-tale-of-two-ports-the-epic-story-of-chinese-direct-investment-in-the-greek-port-of-piraeus/>>.

²⁵ Jack Ewing, 'European Companies Turn to Chinese Investors' *The New York Times* (2014) 1, available at <www.nytimes.com/2014/10/21/business/international/european-companies-turn-to-chinese-investors.html>.

the opportunity to acquire all the European assets at bargain prices, many of which are still for sale at the time of writing.

The main political consequence of the euro crisis on Chinese FDI into Europe was to lessen political resistance and frame its public perception as a “savior” and “white knight”. The crisis has transformed the time horizon of European politics: short-term concerns, above all employment, take precedence over long-term concerns, such as national security. If some European countries, such as France, had displayed an initial wariness about the unique characteristics of Chinese FDI, it dissipated as the impact of the crisis on the French economy became clear. This explains why deals such as the entry of Dongfeng into the capital of French auto maker Peugeot in 2014 were applauded by French politicians when a few years later they probably would have been blocked. Moreover, many European leaders started to actively court Chinese investment, both by stepping up their investment promotion efforts towards China, through state visits and a variety of incentives, and by lowering regulatory hurdles. In some cases, governments tried to encourage directly Chinese individual investors by offering them residency permits and even citizenship in exchange for certain amounts of investment.

Chinese investment has been seen as beneficial to many policy-makers in Europe in the context of the crisis not only because of its immediate impact, such as saving a company from bankruptcy or putting money in the state’s coffers through privatization programs, but also because of its long term economic implications. Most importantly, Chinese investment can be the key for European companies to penetrate the coveted Chinese market. For instance, in 2014 the Chinese company Sanpower Group acquired the venerable British retailer House of Fraser with the objective of launching the brand globally. It now has outlets in China and sells mostly British products there.

In 2016, however, a combination of factors increased the political spotlight and negative perception of some Chinese investment deals in the two biggest destinations for Chinese FDI in Europe. In the UK, the “Brexit” referendum ushered in a new Prime Minister, Theresa May, who questioned publicly the Hinkley Point deal, a project for France’s EDF and China’s CGN to construct a new nuclear power plant in Somerset, England. This provoked a lot of political debate and great media coverage about the soundness of this deal in particular and of Chinese investment in the UK in general. In the end the project was approved in September 2016, with some additional safeguards regarding national security.

In Germany, a series of Chinese investment attempts, some of which also involved the United States, increased the spotlight and the scrutiny on the soundness of accepting so much FDI from China. The proposed takeover of German robot-maker Kuka by Chinese home appliance maker Midea prompted Sigmar Gabriel, German minister of the economy, to propose an expansion of the 2009 Foreign Trade Law (Aussenwirtschaftsgesetz) in order to give the German government more opportunities to review and block certain foreign investments. In November 2016, several Chinese companies expressed interest in investing in Osram, a German company making lighting products and semiconductors. The IG Metall trade union said it would block any deal attempt because of the risks that a potential acquirer would “siphon off Osram’s technology” and shift

production outside Germany.²⁶ In December 2016, the United States blocked the sale of German semiconductor company Aixtron to China's Fujian Grand Chip on the basis that it posed a risk to U.S. security since it could make chips for the Chinese nuclear program.

Overall, attitudes towards Chinese investment remain quite positive throughout Europe. The main concerns are less about direct threats to national security than about the long-term implications for the economic competitiveness of the host country if China acquires technology. One policy response to the new challenge of Chinese investment in the EU would be the creation on a pan-European committee to vet foreign investment –along procedures similar to those used in the United States. The EU acquired institutional competence over foreign direct investment as a result of the 2009 Lisbon Treaty, which would make such a common review process logical, especially since goods and services can circulate freely throughout the single market.²⁷ Indeed, in February 2017, France, Germany and Italy wrote to the EU Trade Commissioner in order to request a European debate over the conditions under which countries would be allowed to investigate and even block foreign investments, especially in the case of sensitive high-tech products or when the investor is state-owned.²⁸ The creation of such a pan-European committee is unlikely in the near future, however, for many reasons. One is that the general political climate is not conducive to further European integration. Another is that the preferences of the various member states on the issue are too disparate –Chinese investment may be regarded by France as an issue of national security and by Germany as a threat to competitiveness, but for other EU countries it is only a welcome source of financing.

Since 2012, the EU and China have been negotiating a Bilateral Investment Treaty (BIT), the first standalone investment agreement with the EU as a party since the granting of the new FDI competence in the Lisbon Treaty. Some of the contentious issues such as market access and transparency of vetting procedures are part of the ongoing talks. Europe's main objective in the negotiations is to obtain reciprocity both on market access and investment protection– such as on access to the Chinese market with no obligation to form joint ventures with local partners, protection for European investments, elimination of state distortions, and increased transparency. As European Commission Vice-President Jyrki Katainen explained, “as we don't have EU-owned companies we cannot [behave] the same [as China].”²⁹ It remains to be seen what will be the impact, on one hand, of the national elections taking place in many EU countries in 2017 –especially in France, Germany and Italy- and, on the other hand, of the U.S. retreat from multilateralism and globalization under the Trump administration on the outcome of the EU-China BIT.

²⁶ Guy Chazan, 'German Labour Union Warns Chinese Suitors over Osram Bid' *Financial Times* (2016) 1, available at <www.ft.com/content/ed463896-aa74-11e6-9cb3-bb8207902122>.

²⁷ Sophie Meunier, 'Integration by Stealth: How the European Union Gained Competence over Foreign Direct Investment' [2017] *Journal of Common Market Studies* 1, available at <<http://onlinelibrary.wiley.com/doi/10.1111/jcms.12528/abstract>>.

²⁸ Guy Chazan, 'EU Capitals Seek Stronger Right of Veto on Chinese Takeovers,' *Financial Times* (2017) 1, available at <www.ft.com/content/8c4a2f70-f2d1-11e6-95ee-f14e55513608>.

²⁹ Janosch Delcker, 'Germany's Chinese Investment Problem' *POLITICO* (2016) 1, available at <www.politico.eu/article/germanys-chinese-investment-problem-sigmar-gabriel-eu/>.

A big question mark also surrounds the consequences of Brexit on Chinese investment in Europe. The UK has been one of the top destinations for Chinese FDI in Europe in recent years. Some of the reasons that pushed Chinese investors towards Britain will still exist after Brexit, such as infrastructure and real estate. However, the attractiveness of the UK for Chinese investors has derived in large part from its participation in the EU Single Market. A “hard Brexit”, whereby the UK will sever its privileged ties to the Single Market, will likely reduce the willingness of Chinese investors to make acquisitions and greenfield investments there and redirect some of this investment, especially in manufacturing, towards EU countries on the continent.

United States: Geopolitical competition and renewed economic nationalism

Perceptions of Chinese investment in the United States are both similar and different to what they have been in Europe. On one hand, Chinese investment has been welcome, especially at the local level, for the same reasons it has been welcome in Europe: as a chance to create or save local jobs through greenfield and acquisitions and an opportunity to tap into the coveted Chinese market. On the other hand, Chinese investment is viewed at the national level with much greater suspicion because of American concern about geo-politics and institutional procedures interpreting foreign investment exclusively through the lens of national security.

Investment from China, as is investment from everywhere, is welcome in the U.S., which is currently the first destination for both stock and flows of FDI in the world. Indeed, the U.S. has long enjoyed a very liberal, “open door” regime towards inward foreign direct investment based on the two guiding principles of absence of government intervention and national treatment for foreign investors.³⁰

At the local level, politicians are not only accepting but also actively encouraging Chinese direct investment. Mayors, state representatives and governors are busy traveling to China and welcoming Chinese officials in the hope of attracting investment. They engage in all kinds of investment promotion and offer a variety of incentives to bring investment to their district. This explains why Chinese FDI in the U.S. has reached record highs, with more than \$50 billion in investment deals in 2016 and 12% of all M&A in the U.S. that year³¹—major deals such as the purchase of General Electric’s appliances unit by Haier (\$5.4 billion) and the acquisition of the Legendary Entertainment studio by Dalian Wanda (\$3.5 billion) but also a multitude of small deals.

At the national level, the picture is more complicated. Over several decades, foreign investments entering the U.S. have become increasingly vetted and restrictive in response to successive episodes of backlash. The procedure in effect today requires the executive branch to screen incoming foreign investments and potentially to suspend or prohibit mergers and acquisitions. This is accomplished through a review process done by the Committee on Foreign

³⁰ Daniel H. Rosen and Thilo Hanemann, 'An American Open Door?,' *Maximizing the Benefits of Chinese Foreign Direct Investment* (2011) 1.

³¹ Ellen Sheng, 'Chinese Investment In U.S. Hits Record High Of \$18.4 Billion In First Half Of 2016,' *Forbes* (2016) 1, available at <www.forbes.com/sites/ellensheng/2016/07/25/chinese-investment-in-u-s-hits-record-high-of-18-4-billion-in-first-half-of-2016/> accessed July 25, 2016.

Investment in the United States (CFIUS), an interagency committee including officials from the departments of Commerce, Defense, Homeland Security, State, and USTR, among others.³² The review process applies to foreign investment in the U.S. as well as to foreign investment in foreign companies that have affiliates in the U.S. According to the latest official CFIUS records for 2012-2014, China was the home country of the largest number of deals that went through the CFIUS process, followed by the United Kingdom, Canada, Japan, and France.³³ Chinese acquisitions are investigated more thoroughly because many of the potential investors are either State-Owned Enterprises or have close ties to the Chinese government. In 2016, CFIUS blocked, among others, the acquisition of Philips' Lumileds by Chinese private equity investors and of German chip maker Aixtron by China's Fujian Grand Chip Investment on national security grounds.

If the Executive is the only branch responsible for the FDI approval process through CFIUS, Congress has been the locus of the heaviest politicization of investment deals over the years. Either out of genuine concern for American national security or to score political points by posturing, Congressional members may hold hearings and pass new legislation to restrict foreign investment.³⁴ They can also simply complain loudly and publicly about foreign investment in speeches, interviews, or campaign ads.

As a result of these procedures and practices governing the politics of foreign investment in the U.S., concerns for national security have been the principal lens through which Chinese FDI has been perceived at the national level in the U.S. over the past decade. While it has captured the attention of the media and has drawn complaints by Chinese officials, it does not reflect the efforts that have been deployed at the local level to favor and expand Chinese investment.

The impact of the 2016 American election is still uncertain at the time of writing. On one hand, the tone of discourse emanating from President Trump has been initially more belligerent towards China in general and the Chinese economy in particular. He may direct his administration to review incoming foreign investments more broadly and thoroughly through the CFIUS process and insist more forcefully on reciprocal access for American firms in China. Chinese investments are more likely to be scrutinized and decried in the political arena. Indeed, some bipartisan efforts are already underway in Congress to tighten scrutiny of Chinese investments into the U.S., for instance with special provisions for high-technology deals or with an expansion of the CFIUS mandate to include economic factors when assessing foreign takeovers.³⁵ On the other hand, getting more direct investment into the U.S. will be crucial to Trump's objective of repatriating jobs and "Make in America" again.

³² James K. Jackson, *The Committee on Foreign Investment in the United States (CFIUS)* (Congressional Research Service, 2014) 1.

³³ CFIUS, 'Committee on Foreign Investment in the United States Annual Report to Congress CY2014' (2016) 1.

³⁴ Rosen and Hanemann, 'An American Open Door?,' *Maximizing the Benefits of Chinese Foreign Direct Investment* (2011) 1

³⁵ Kate O'Keeffe, 'Lawmakers Push for Tighter Scrutiny of Chinese Investment in U.S.,' [2017] *Wall Street Journal* 1. Politics, available at <www.wsj.com/articles/lawmakers-push-for-tighter-scrutiny-of-chinese-investment-in-u-s-1487678403>.

IV. CONCLUSION: BEWARE OF CHINESE BEARING GIFTS?

Why do these political challenges matter? Because they are ultimately a central factor in determining the success of an investment –no matter how good is the business plan, the due diligence, or the financial backing, the foreign investment is not going to succeed in the end if the host government blocks the transaction or public opinion initiates backlash. Whether Chinese investments are interpreted as novel or unique do influence the type of political reception they receive in the host country –the more idiosyncratic they are perceived to be, the more likely they are to trigger political controversy and the creation of more stringent FDI vetting mechanisms.

Several recent developments will determine how much Chinese direct investment will continue to grow in Europe and the U.S. over the next few years and whether they will be welcomed or treated as a potential Trojan Horse. For one, the Chinese government has imposed in late 2016 tighter controls on outbound investment, notably for Chinese companies undertaking major acquisitions of foreign firms unrelated to their core business, and established stricter approval requirements for cross-border deals over 10 billion dollars. Designed to curb capital flight, these new measures might transform the nature of the investment deals done in Europe and the U.S. and increase the number of deals undertaken by private investors.

Another recent development has been the creation of the “Made in China 2025” initiative by the Ministry of Industry and Information Technology. The objective is to upgrade Chinese industry and move it up the global value chain, notably by encouraging innovation, strengthening intellectual property rights, and nurture human talent. Outbound Chinese FDI is likely to play a role in implementing this initiative. In the short term, this should increase Chinese efforts to invest in Europe and the U.S., especially in sectors with superior technology and know-how, which should have a positive impact on the host economies. In the long term, however, this will accelerate the competitiveness of Chinese industry.

On the host country side, one recent development related to the “novel” vs. “unique” dichotomy has been the publicization of some notable successes of Chinese investments. Initial media reports about new incoming Chinese investments in Europe and the U.S. were most often focused on failures and mistakes, such as CNOOC’s failed attempt to take over Unocal in 2005. Recently, however, now that Chinese FDI has been around for almost a decade, many articles are focusing on examples of successes, for instance in the case of big profile deals such as Geely’s acquisition of Volvo and COSCO’s management of Piraeus. Successful smaller acquisitions have also been featured in the media, such as Putzmeister, “a German maker of pumps for concrete, [which] has seen its workers’ jobs secured and its sales rise nearly a third since Chinese competitor Sany bought it in 2012.”³⁶ Indeed, Chinese investors have been careful not to provoke

³⁶ Paul Carrel and others 'Don't Expect Trump-Style Protectionism from Germany' Reuters (2017) 1, available at <www.reuters.com/article/us-germany-china-m-a-analysis-idUSKBN14T1IO>.

political backlash, which has happened thanks to a learning curve coupled with a clear Chinese strategy that has involved relying on Western public relations and legal firms to smooth out deals.

The simultaneous negotiations of bilateral investment treaties between China and the EU, on one hand, and the U.S., on the other, will also determine the nature and amount of future Chinese outbound FDI. Western countries are particularly concerned about hurdles to market access caused by a lack of reciprocity. China invested \$37 billion in the EU in 2016, while European countries invested only \$8.5 billion, dropping for a fourth straight year.³⁷ If no progress is made on making Western investments into China as easy as Chinese investments in Western countries, Europe and the U.S. may tighten inbound investment regulations and make it more difficult for Chinese investors to make deals.

Finally, the politics of hosting Chinese investments will also depend on which other countries are trying to invest in local companies. As other potentially politically problematic countries, such as Russia and Qatar for instance, try to invest in Europe and the U.S., Chinese investment may become more politically desirable by comparison.

³⁷ Thilo Hanemann and Mikko Huotari, 'Record Flows and Growing Imbalances: Chinese Investment in Europe in 2016' Merics Papers on China (2017) 1, available at <www.merics.org/fileadmin/user_upload/downloads/MPOC/COFDI_2017/MPOC_03_Update_COFDI_Web.pdf>.