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Buying Influence? An Analysis of the Political and Economic Impacts of Chinese Foreign Direct Investment in the European Union

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Abstract

This thesis analyzes the economic and political impacts of the recent influx of Chinese outward foreign direct investment (OFDI) into the European Union (EU). I consider the ways in which EU perceptions of Chinese OFDI have evolved over the course of the past decade as well as what attempts the EU has made at an institutional level to address challenges posed by Chinese investment. I contend that despite institutional efforts to respond to these perceived challenges – namely losing a technological edge, security concerns, and unreciprocated market access – Chinese OFDI in the EU has had a divisive effect. Not only has Chinese OFDI exacerbated economic cleavages within the bloc, but China has parlayed its economic relationship with many smaller EU member states into political leverage.

Keywords: China, EU, FDI, investment screening, security, political influence

Table of Contents

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Introduction

The rise of China, as an economic, political, and military power, has become a primary focus of the international community over the past two decades. The spotlight on China is understandable, given its unprecedented transformation from a poor, communist, and highly agrarian country to the world's largest economy – in purchasing power parity (PPP) terms – in the span of only forty years. In fact, it is China's economic growth – which the World Bank dubbed "the fastest sustained expansion by a major economy in history"[1] – that has turned heads across the globe. While China's economic ascendancy has been impressive in and of itself, the nature of China's dramatic turnaround is equally as remarkable. The economic reforms that started under Deng Xiaoping flew in the face of the orthodox policy prescriptions trumpeted by the West. Instead, China has taken a hybrid approach to economic development, combining the power of local entrepreneurship with heavy-handed state planning to great effect.

For years, Western countries welcomed China into the international fold, despite the persistence of a nominally communist government and a heterodox approach to economic development. There was a pervasive current of thought that China's mixed economic system was a temporary step in the inevitable process of full liberalization; as China grew more prosperous it would slowly conform to the Western rules-based order. China has indeed grown more prosperous, but prosperity has not ushered in the sort of economic and political reforms

[1] "The World Bank in China," World Bank, accessed March 24, 2020, https://www.worldbank.org/en/country/china/testpagecheck.

that many Western leaders had hoped for. Rather, China has shown its ambitions to become a world superpower, transitioning from a rule taker to a rule maker. Consequentially, Western leaders on both sides of the Atlantic have looked upon Beijing's model of capitalism with Chinese characteristics more critically. The same economic policies that have yielded tremendous growth within China have been increasingly perceived as tools of economic statecraft that often work to the detriment of everyone else.

In the US, much of the conversation about Chinese economic statecraft has revolved around trade, and in particular, the US's trade deficit with China. Starting with Bill Clinton in 1994, US leaders have consistently identified China as, if not openly accused them of, being currency manipulators to keep the renminbi artificially undervalued.[2] In recent years the issue has become more contentious with President Trump taking a brasher line against Beijing and instigating a "trade war" of retaliatory tariffs. In Europe, while trade relations with China continue to be a main concern of the European Union (EU), a new facet of the bloc's economic relationship with China has gained prominence in national and supranational conversations: foreign direct investment (FDI).

According to the Organization for Economic Cooperation and Development (OECD), FDI is defined as "a category of cross-border investment made by a resident in one economy (the direct investor) with the objective of establishing a lasting interest in an enterprise that is resident in an economy other than that of the direct investor."[3] It can be difficult to measure

[2] Brad Sester, "How Not to Fight a Currency War," *Foreign Affairs*, August 28, 2019, https://www.foreignaffairs.com/articles/china/2019-08-28/how-not-fight-currency-war.
[3] "OECD Benchmark Definition of Foreign Direct Investment" (OECD Publishing, 2008), https://www.oecd.org/daf/inv/investmentstatisticsandanalysis/40193734.pdf.

what investments are and are not encompassed by the term FDI, as evidenced by the OECD's 254-page benchmark definition of FDI, but broadly speaking FDI takes two forms. Foreign firms may acquire an enterprise or a controlling share of an enterprise in the host country, known as mergers and acquisitions (M&A), or foreign firms may directly establish business operations in the host country, which is referred to as greenfield investment. Importantly, portfolio investments are not considered FDI.

Outward foreign direct investment (OFDI) from China may appear to be a relatively uncontroversial issue, yet it is anything but. On a broader level, receiving FDI from any country is both an economically and politically challenging prospect. While there are undoubtedly benefits to hosting FDI, such as increased economic activity in the host country, greater levels of trade with the country of investment origin, and possible gains in innovation and human capital, these benefits must be considered along with potential drawbacks, namely the crowding out of domestic investment, negative influence on exchange rates, and loss of control of key industries. This calculus has become particularly important when considering OFDI from China. As China has extended its FDI footprint around the world, especially under the umbrella of the Belt and Road Initiative (BRI), their intentions as well as the quality and implications of the investments have been called into question.

While the EU, which is the world's second largest economy in both nominal and PPP terms, has not traditionally been at the center of China's plans to expand its outward investment, it now finds that it too must reckon with the advent of Chinese OFDI. And though the 27-member bloc of countries does not face the same set of challenges in addressing the inrush of Chinese capital as do many smaller, less-developed nations in Southeast Asia and

Africa, significant challenges exist nonetheless. These challenges cut across economics, politics, and security, and are forcing the EU to grapple with questions concerning its collective identity and ability to balance priorities. In short, Chinese OFDI already has, and will continue to have, a significant impact on the EU.

Whereas there is a large body of work addressing general China-EU relations, academic work investigating the impact of Chinese OFDI in the EU is less robust. The majority of China-EU research examines the evolving nature of the EU and China's relationship vis-à-vis a number of subject areas, such as the environment, security, governance, and commercial relations. Even within the subset of literature that focuses specifically on Chinese OFDI in the EU there is a relative dearth of work addressing how Chinese investment practices are reshaping EU-China relations and intra-EU relations in particular. For example, a number of authors consider Chinese OFDI practices from a business perspective, explaining investment rationale and trying to predict what factors motivate Chinese firms to move operations abroad.[4] Others, notably Thilo Hanemann,[5] have kept their analysis to a quantitative level without exploring the ramifications of increased Chinese FDI in depth.

There are, however, a number of academic articles that have begun to delve into the political dimension of hosting Chinese FDI in the EU. Sophie Meunier has been the most prolific writer in this field, publishing a succession of articles assessing the political repercussions of

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4 *See, for example:* Xiaoxi Zhang and Kevin Daly, "The Determinants of China's Outward Foreign Direct Investment," *Emerging Markets Review* 12, no. 4 (December 2011): 389–98, https://doi.org/10.1016/j.ememar.2011.06.001; Xueli Huang and Chi Renyong, "Chinese Private Firms' Outward Foreign Direct Investment: Does Firm Ownership and Size Matter?," *Thunderbird International Business Review* 56, no. 5 (2014): 393–406, https://doi.org/10.1002/tie.21629.

5 Thilo Hanemann, "Chinese Direct Investment in the EU and the US: A Comparative View," *Asia Europe Journal* 12, no. 1 (March 1, 2014): 127–42, https://doi.org/10.1007/s10308-014-0379-5.

Chinese OFDI in the EU. Articles from Nicolas[6] as well as Knoerich and Miedtank[7] have also considered bloc-wide implications of Chinese OFDI. Other authors have focused specifically on Chinese OFDI in Central and Eastern European (CEE) countries,[8] BRI investment across the bloc,[9] or the EU's regulatory policies in response to Chinese investment.[10]

Outside of academia, there is no short supply of commentary on Chinese OFDI in the EU originating from think tanks and journalists. The European Council on Foreign Relations (ECFR), Bruegel, and a number of smaller national or regional think tanks have pushed out commentary and reports on Chinese investment practices, while *The Guardian*, *The Financial Times, The New York Times* and *The Economist* have all covered the topic to varying degrees. The greater amount of coverage that Chinese OFDI in the EU has received by think tanks and the media is in part a reflection of the novel and highly dynamic nature of these investments; in the past decade the Chinese OFDI landscape has shifted considerably. As such, this thesis looks to add to the limited literature surrounding Chinese OFDI in the EU, paying particular attention to how Chinese investment is altering the EU's internal dynamics.

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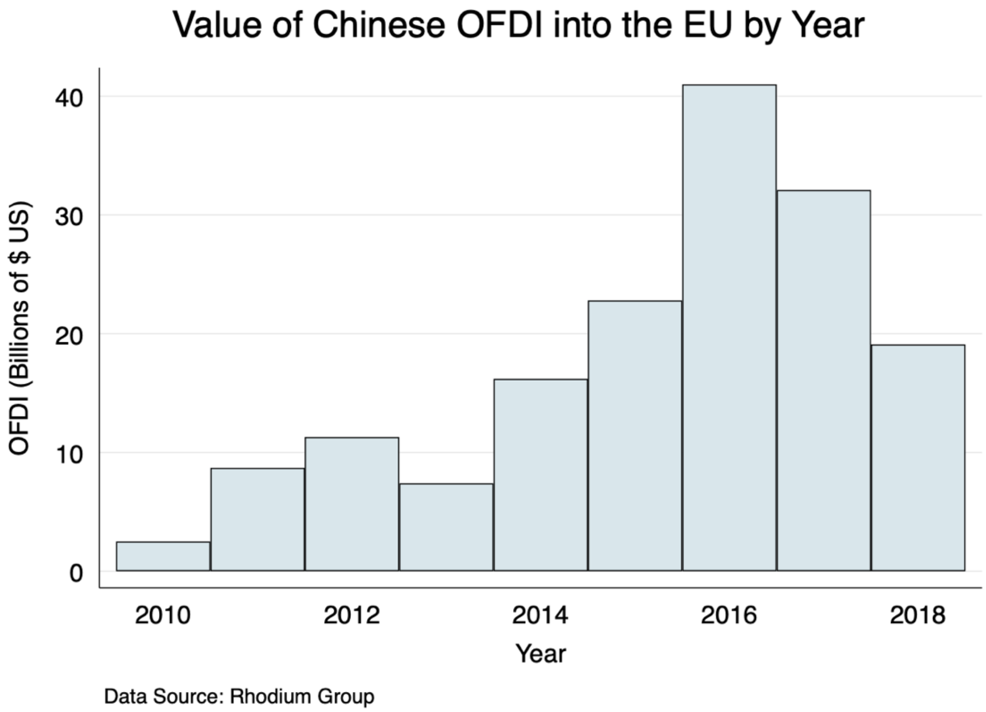
[6] Françoise Nicolas, "China's Direct Investment in the European Union: Challenges and Policy Responses," *China Economic Journal* 7, no. 1 (January 2, 2014): 103–25, https://doi.org/10.1080/17538963.2013.874070.
[7] Jan Knoerich and Tina Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe," *CESIFO Forum* 19, no. 4 (December 2018): 3–8.
[8] *See, for example:* Wade Jacoby, "Different Cases, Different Faces: Chinese Investment in Central and Eastern Europe," *Asia Europe Journal* 12, no. 1 (March 1, 2014): 199–214, https://doi.org/10.1007/s10308-014-0380-z; Ágnes Szunomár and Agnieszka McCaleb, "Chinese and Other East Asian Foreign Direct Investment in Central and Eastern Europe: Motives, Location Choices and Employment Approaches," *CESIFO Forum* 19, no. 4 (December 2018): 9–14.
[9] Zuokui Liu, "Europe's Protectionist Position on the Belt and Road Initiative and Its Influence," *China International Studies* 72 (2018): 145–65.
[10] Haiyan Zhang and Daniel Van Den Bulcke, "China's Direct Investment in the European Union: A New Regulatory Challenge?," *Asia Europe Journal* 12, no. 1/2 (March 2014): 159–77, https://doi.org/10.1007/s10308-014-0383-9; Frank Bickenbach and Wan-Hsin Liu, "Chinese Direct Investment in Europe – Challenges for EU FDI Policy," *CESIFO Forum* 19, no. 4 (December 2018): 15–23.

Specifically, Chapter I will outline the trends in Chinese OFDI in the EU, paying particular attention to investment volume, the geographical distribution of investment, and what form Chinese investment tends to take. Chapter II will then contextualize these investment trends by examining Chinese motivations for investing in the EU. This chapter will consider business investment literature as well as the historical and political circumstances in both China and the EU that help account for the unique trends in Chinese OFDI in the EU. Chapter III will then turn to how the EU has reacted to the influx of Chinese OFDI at an institutional level. In particular, this chapter will focus on the specific challenges that Chinese OFDI poses to the bloc and what efforts the EU has made to address them. Chapter IV will examine the differences in member state opinion toward the challenges and benefits of Chinese OFDI, demonstrating how increased levels of investment have deepened economic cleavages in the bloc. Finally, chapter V will then consider how Chinese OFDI has not only harmed the economic cohesiveness of the EU but its political cohesiveness as well.

Chapter I – Chinese OFDI Trends in the EU

The rise in Chinese OFDI into the EU over the past decade has been truly remarkable. Prior to the global financial crisis (GFC), which mired most of the Eurozone in economic stagnation, China's level of investment in the EU was negligible. In fact, from 2004 to 2008, Chinese OFDI in Europe totaled less than $1 billion annually. However, in the wake of the crisis, Chinese investment into the EU tripled, as roughly $3 billion entered the EU from China in both

2009 and 2010.[11] This explosion of investment continued into the next decade, with inflows again tripling by 2012 and eventually peaking at $41 billion in 2016.[12]



Interestingly, Chinese OFDI in the EU has been in sharp decline since 2016. From 2016 to 2017 Chinese investment dropped from $41 billion to $32.1 billion. 2018 saw a similar decrease in Chinese investment, representing the lowest level of investment since 2014 and over a 50% decrease in investment from 2016.[13] Though full data are not yet available, similarly low levels

[11] Sophie Meunier, "'Beggars Can't Be Choosers': The European Crisis and Chinese Foreign Direct Investment in the European Union," *Journal of European Integration* 36, no. 3 (2014): 283-302.
[12] Thilo Hanemann, Mikko Huotari, and Agatha Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies" (Rhodium Group and Mercator Institute for China Studies, March 2019), https://rhg.com/wp-content/uploads/2019/03/RHG-MERICS-COFDI-Update-2019.pdf.
[13] Ibid.

of Chinese OFDI in the EU are expected in 2019. Not only has Chinese OFDI into the EU been decreasing in the past few years, but China divested over $4 billion worth of European assets since 2016.[14] Despite the recent pullback in Chinese investment into the EU, China remains a significant source of investment for the EU as a whole. The United States, Canada, and European Free Trade Association (EFTA) countries such as Switzerland and Norway have consistently accounted for the majority of OFDI into the EU, but since 2007 China has solidified itself as a top investor in the region. A working document from the European Commission found that China controls approximately 28,000 EU-based firms and 1.6% of the assets of EU-based firms. This represents a significant increase from a decade earlier, when China controlled only 5,000 firms and .6% of assets.[15]

China has turned heads as an investor in the EU not only because of the huge increase in quantity of investment in a short timeframe, but because of the character of Chinese investment. Compared to investment from other countries, a large proportion of Chinese investment is made by state-owned enterprises (SOEs). The EU classifies SOEs as firms with at least 20% government ownership, but this cut-off may not accurately capture the extent of state-backed investment in the EU; it is often difficult to determine the level of government involvement in many Chinese firms and therefore to what extent these firms are under influence from the state. Using the formal definition of a SOE, the EU estimates that since 2000, over 60% of all Chinese OFDI in the EU originated from these government-backed enterprises.[16]

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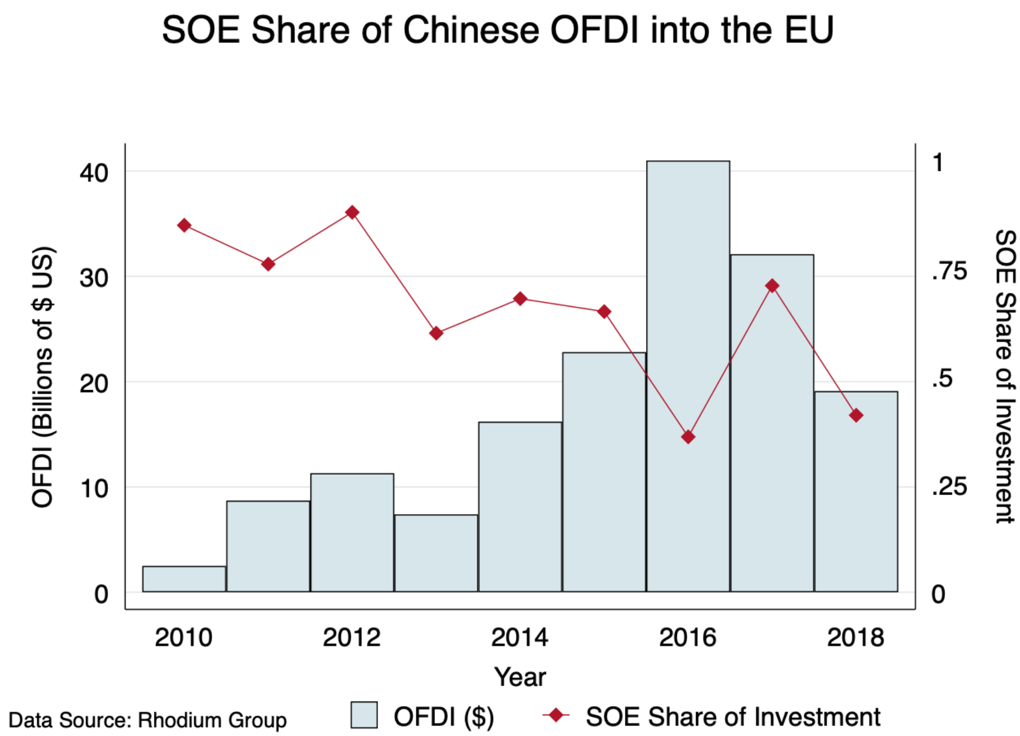
[14] Ibid.

[15] European Commission, "Commission Staff Working Document on Foreign Direct Investment in the EU," Working Document (Brussels, March 13, 2019), https://trade.ec.europa.eu/doclib/docs/2019/march/tradoc_157724.pdf.

[16] Ibid.

Chinese SOEs' share of investment peaked in the early 2010s, when upwards of 75% of all investment was made by SOEs. While this share has decreased to 41% in 2018, the SOE share of investment is still unusually large compared to other regions investing in the EU.[17] In fact, in 2017, only EFTA countries saw a larger share of their OFDI into Europe originate from SOEs.[18]



Around 95% of Chinese SOE investment in the EU takes the form of mergers and acquisitions. This preference for M&A rather than greenfield investment has been fairly consistent in the past decade, as Chinese firms have looked to capitalize on existing firm

[17] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."
[18] European Commission, "Commission Staff Working Document on Foreign Direct Investment in the EU."

infrastructure and knowhow.[19] Noticeably, Chinese SOE investment in the EU is concentrated in a handful of strategic sectors, such as utilities, machinery, and transportation services and infrastructure. As the European Commission highlights, this concentration of investment is driven primarily by a number of mega-deals within those sectors by some of China's largest SOEs, such as China Investment Corporation (CIC), Three Gorges, State Grid, and ChemChina.[20] When broadening the scope of Chinese OFDI to include private investment, a similar preference for M&A investments rather than greenfield projects is evident, but there is less of a sectoral focus on utilities, machinery, and transportation. Once again, in previous years, the prevalence of mega-deals, such as Tencent Gaming's $8.6 billion acquisition of Supercell, disproportionately weights investment in certain sectors.[21] In 2018 however, due in part to a lack of mega-deals, no single sector accounted for more than 20% of total Chinese investment.[22] Increased investment in biotech, health, and business and financial services contributed to this industry diversification of investment as well.

Though all EU member states have been recipients of Chinese OFDI, the geographic distribution of investment has been very uneven. The large economies of Western Europe have received the largest share of Chinese investment, with the UK leading the way at approximately $51.5 billion transacted since 2000.[23] Germany and France, who round out the "Big Three" economies, have consistently been favorite destinations for Chinese OFDI. In recent years investment in the Benelux countries and Northern Europe has increased. Investment in

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[19] Knoerich and Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe."
[20] European Commission, "Commission Staff Working Document on Foreign Direct Investment in the EU."
[21] Andre Tartar, Mira Rojanasakul, and Jeremy Scott Diamond, "How China Is Buying Its Way Into Europe," Bloomberg.com, April 23, 2018, https://www.bloomberg.com/graphics/2018-china-business-in-europe/.
[22] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."
[23] Tartar, Rojanasakul, and Jeremy Scott Diamond, "How China Is Buying Its Way Into Europe."

Southern and Mediterranean Europe has fallen to under 15% of total Chinese OFDI in the EU, well below its peak of around 40% of investment in the years 2012-2015. Central and Eastern Europe has seen the lowest levels of Chinese OFDI, not accounting for more than 5% of investment into the EU in any given year since 2013.[24] Despite the low level of overall Chinese investment in CEE countries, greenfield investment in the region has actually seen an uptick. Chinese firms have invested in the construction of solar farms in both Hungary and The Czech Republic as well as an automotive R&D center in Austria and a manufacturing plant in Poland.[25]

Chinese regional investment patterns may seem intuitive, given the size of the economies that comprise each region. China is investing most heavily in the larger, more developed economies of Western and Northern Europe. However, the volume of Chinese OFDI has not always been proportional to the size of the recipient economy. When taking into consideration the 2018 GDP of each member state in addition to the volume of Chinese investment into each economy, it is clear that certain countries have received a disproportionate amount of Chinese investment. For example, though Malta has only received .5% of all Chinese OFDI into the EU since 2000, the roughly $880 million worth of investment from China is equal to just over 6% of the country's 2018 GDP. Conversely, though Germany has received roughly $24.4 billion in Chinese investment since 2000 (14.6% of all Chinese OFDI into the EU during that period), this total is equivalent to only .56% of Germany's 2018 GDP.

[24] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."
[25] Szunomár and McCaleb, "Chinese and Other East Asian Foreign Direct Investment in Central and Eastern Europe: Motives, Location Choices and Employment Approaches."

Country	Chinese OFDI ($B)	OFDI as share of 2018 GDP
Malta	0.88	0.0607
Luxembourg	2.64	0.0384
Finland	8.03	0.0292
Portugal	1.54	0.0277
UK	51.59	0.0182
Hungary	2.64	0.0170
Sweden	6.71	0.0122
Netherlands	10.89	0.0119
Greece	2.09	0.0095
Cyprus	0.22	0.0090

Table 1 - 10 Largest EU Recipients of Chinese OFDI Measured as a Share of Their 2018 GDP (Data Source: Rhodium Group)

The ten EU member states who received the most Chinese OFDI as a share of their 2018 GDP are quite diverse, economically and geographically. Five are advanced economies in Western and Northern Europe, two are small Mediterranean island nations, two are medium-sized Southern European economies, and one is located in Central Europe. The type of Chinese investment made into each country is not identical. Notably, most Chinese investment in Luxembourg has been in financial services or what the IMF would classify as “phantom FDI” – investment into shell companies in tax havens.[26] On the other hand, Chinese investment in Greece has been focused in the energy and shipping sectors, most remarkably China Ocean Shipping Company’s (COSCO) purchase of the Port of Piraeus in 2009.

One form of Chinese OFDI that has garnered significant attention from governments and political commentators alike is BRI investment. Launched in 2013, BRI is a sweeping and

[26] Jannick Damgaard, Thomas Elkjaer, and Niels Johannesen, “The Rise of Phantom Investments,” *Finance & Development (IMF)* 56, no. 3 (September 2019): 11-13.

ambitious foreign policy project that Chinese President Xi Jinping has lauded as "the project of the century."[27] Substantively, BRI looks to leverage China's unrivaled capabilities in construction to undertake huge infrastructure and connectivity projects across the globe. Most of China's BRI investment has been focused in Southeast Asia, but in recent years, Africa, Central Asia, Latin America, and Europe have all seen an uptick in BRI-related investment. The initiative has received an enormous amount of attention, in large part do the ambiguity inherent in Xi's signature project. The lofty language in which BRI is couched, such as being labeled "the integration of spiritual and material human abilities to understand the world, change the world, and profoundly shape the destiny of humanity," by Chinese policy advisers at Tsinghua University, does little to disentangle the initiative's true intentions.[28]

The ambiguity surrounding BRI and what does or does not count as a BRI project make measuring its presence in the EU difficult. Indeed, there is no official list of BRI projects currently underway in the EU, despite the fact that the majority of EU member states have signed non-binding Memoranda of Understanding (MoU) with China regarding the initiative. Thus, estimations of the quantity of BRI investment in the EU varies according to the analyst. For example, The Mercator Institute for China Studies' (MERICS) BRI database includes all investments valued at $25 million or greater that further BRI policy goals, whether or not they receive the official BRI rubber stamp. The American Enterprise Institute's (AEI) China Global Investment Tracker uses slightly different criteria, considering all infrastructure investment in

[27] Yuen Yuen Ang, "Demystifying Belt and Road," *Foreign Affairs*, May 22, 2019, https://www.foreignaffairs.com/articles/china/2019-05-22/demystifying-belt-and-road.
[28] Angang Hu and Xin Zhang, "'Belt and Road': A Century Project to Build a Blessing for All," China Daily, May 2017, http://china.chinadaily.com.cn/2017-05/16/content_29371140.htm.

EU member states that China recognizes to be part of BRI (even if the host country does not claim to be part of BRI) as BRI investment. One project that all parties, including the EU itself, agree constitutes a BRI project is the Belgrade-Budapest railway. Currently under construction, the nearly $3 billion project will first connect the Hungarian and Serbian capitals, before eventually being extended down to the Chinese-owned Port of Piraeus.[29] Beyond this hallmark project, which investments should or should not be classified as BRI investment is disputed, though there seems to be consensus that the volume of BRI investment in Europe is still relatively low compared to other regions.

In summary, Chinese OFDI in the EU over the past decade has been quite idiosyncratic. In the wake of the GFC, Chinese investment in the EU has increased significantly yet waned in recent years. Similarly, the SOE share of investment remains high, but has decreased noticeably since the peak years of the early 2010s. In terms of investment volume, most Chinese OFDI is directed towards the EU's most robust economies, and the UK in particular, with the CEE region receiving the lowest share of investment. The assortment of member states that have received disproportionate shares of Chinese OFDI is much more varied, however. Furthermore, the effect of China's BRI, announced seven years ago, has been difficult to gauge. There have been a number of high-profile Chinese-backed infrastructure projects in the EU, but it seems the initiative's biggest impact has been to cause confusion and trepidation throughout the bloc.

[29] Wade Shepard, "Another Silk Road Fiasco? China's Belgrade To Budapest High-Speed Rail Line Is Probed By Brussels," Forbes, February 25, 2017, https://www.forbes.com/sites/wadeshepard/2017/02/25/another-silk-road-fiasco-chinas-belgrade-to-budapest-high-speed-rail-line-is-probed-by-brussels/.

Chapter II – China's Investment Motivations

While Chinese OFDI into the EU can be characterized as idiosyncratic, the patterns of investment volume, type, and location fall in line with China's evolving geoeconomic strategies. A propitious investment environment in Europe following the GFC paired with a broader Chinese ambition to move production up the value chain contributed to the huge surge in Chinese OFDI into the EU.

With the GFC miring most of the EU in an extended period of economic stagnation, many countries saw FDI as a key source of capital to jumpstart growth. Pervasive double-digit unemployment and fiscal frugality left governments cash-strapped. But because European banks responded to the crisis by holding onto assets and securing their balance sheets, capital was scarce within the EU itself.[30] A lack of willing European investors and unfavorable short-term economic prospects throughout the EU severely dampened investment demand.[31] Not only did investment demand decrease, but the supply of investment opportunities sharply increased. A number of large infrastructure projects were opened to private bidders and in some cases heavily indebted governments were placed on privatization plans by bailout agencies. Such was the case in Greece and Portugal where everything from ports and railways to state owned airlines were put up for sale.[32] The burgeoning supply of investment opportunities yet plummeting demand led to decreased valuations of European assets,

[30] Meunier, "'Beggars Can't Be Choosers': The European Crisis and Chinese Foreign Direct Investment in the European Union."
[31] Jeremy Clegg and Hinrich Voss, "Chinese Overseas Direct Investment in the European Union" (London: ECRAN, 2012), https://www.chathamhouse.org/sites/default/files/public/Research/Asia/0912ecran_cleggvoss.pdf.
[32] Meunier, "'Beggars Can't Be Choosers': The European Crisis and Chinese Foreign Direct Investment in the European Union."

essentially creating a litany of economic “bargain basement” opportunities.[33] Chinese SOEs and private firms capitalized on the economic opportunities in the EU, snapping up real estate and undervalued European firms alike.

Going Global

The explosion of Chinese investment in the EU, however, cannot be solely attributed to naked opportunism in the wake of the GFC. The two and a half decades of blistering Chinese growth experienced after Mao Zedong’s death were due to extensive market-based reforms within China, yet the country remained a largely closed economy during this period. At the turn of the millennium China began changing tact, strategically reorienting its economy outward as part of its “go global” strategy. China acceded to the World Trade Organization (WTO) in 2001, officially opening its economy to some competition and foreign investment. Of equal importance was Premier Rongji’s announcement of China’s tenth five-year plan in March of 2001. Among the raft of strategic goals and economic reforms elucidated in the plan, Rongji recognized the importance of international integration and encouraged Chinese enterprises to “go outside.”[34] Specifically, Rongji signaled that OFDI was an explicit policy goal by exhorting “enterprises with comparative advantages to make investments abroad, to establish processing operations, to exploit foreign resources with local partners, to contract for international

[33] Ibid.

[34] Zhu Rongji, “Report on the Outline of the Tenth Five-Year Plan for National Economic and Social Development (2001),” March 5, 2001, http://www.gov.cn/english/official/2005-07/29/content_18334.htm.

engineering projects, and to increase the export of labor."[35] The Chinese government did in fact change policy to facilitate outward investment by Chinese firms. Most notably, they relaxed outbound capital controls and streamlined approval procedures for firms looking to expand abroad.[36]

The reasons for a change in Chinese attitude towards OFDI are multifaceted, and satisfy a variety of strategic goals. From a macroeconomic stability perspective, OFDI helped China solve a balance of payments conundrum. For years the state had amassed a wealth of foreign reserves, especially US treasury bonds, but wanted to avoid revaluing the renminbi.[37] Outward investment went a long way to ease these upwards currency pressures. OFDI also assuaged trade tensions. WTO accession put Chinese growth tactics in the international limelight, and many countries accused China of flooding markets with cheap goods. Opening manufacturing facilities abroad was an easy remedy for these recurring frictions. For example, the appliance manufacturing conglomerate Haier Group opened production facilities in Europe and the United States to avoid quota restrictions, anti-dumping sanctions, and a general animus toward Chinese goods.[38]

While avoiding anti-dumping sanctions and keeping the renminbi undervalued were important goals, China's "go global" policy is above all else a strategy to move production up the global value chain. China relied on cheap labor and low-cost exports to drive much of its initial growth, but has recognized the importance of developing higher value-added industries

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[35] Ibid.
[36] *OECD Investment Policy Reviews: China 2008: Encouraging Responsible Business Conduct* (OECD, 2008), https://doi.org/10.1787/9789264053717-5-en.
[37] Ibid.
[38] Ibid.

to spur on further growth.[39] In short China does not want to simply import components for final product assembly, but create these products domestically. Doing so requires a confluence of factors, such as the acquisition of advanced technology and managerial knowhow, both of which are available in spades in European markets. In fact, China's desire to acquire advanced technology and managerial knowhow in order to upgrade firm capacity helps explain why Europe has been a major destination for OFDI and why the vast majority of investment has taken the form of M&A.[40]

Globally, the majority of FDI follows the pattern of firms from advanced economies expanding into countries with equally developed or less developed economies. The main motive is market-seeking, and firms will use their ownership advantages, such as superior technology, greater brand recognition, or managerial advantages, to do so.[41] Much of China's OFDI has followed this pattern, with the largest share of its OFDI being funneled into less developed Asian economies.[42] But Chinese investment into the EU breaks from the paradigm. Chinese firms, both state-owned and private, are investing in more advanced economies as a form of strategic asset-seeking, most notably to acquire European technology and managerial prowess.[43]

In terms of technology, the tenth five-year plan referenced both "enhancing traditional industries with high, new and advanced technologies," as well as "developing new and high-

[39] William H. Overholt, *China's Crisis of Success* (Cambridge: Cambridge University Press, 2018).
[40] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."
[41] Knoerich and Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe."
[42] *OECD Investment Policy Reviews: China 2008: Encouraging Responsible Business Conduct*.
[43] Knoerich and Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe."

tech industries" as key goals.[44] Subsequent five years plan, and most recently Premier Li Keqiang's "Made in China 2025" policy, have employed similar verbiage to describe Chinese ambitions in advanced technology as well. As a late developer, the task of rapidly building up advanced technological capacities has not been lost on the Chinese government. Indeed, China has realized that the quickest and least expensive way to acquire advanced technologies is to buy a company that owns this technology, rather than painstakingly, and perhaps illegally, try to develop it oneself.[45] Thus, many Chinese firms have used investment in the EU as a form of strategic asset-seeking, looking to acquire and transfer new technological capabilities in order to address the technological weaknesses of Chinese firms.[46] Some notable examples of Chinese attempts to facilitate technology transfers from European firms range from Midea's acquisition of Kuka Robotics, China Investment Corporation's (CIC) acquisition of NXP Semiconductors' RF Power unit, and Wanhua's acquisition of Borsod Chemical.[47] Each of these deals was quite large (worth over $1B) and highlights the diversity of technological sectors into which Chinese firms have invested.

Chinese strategic asset-seeking in the EU has not only targeted physical assets such as technologies, but also intangible assets like managerial knowhow and brand recognition. Many Chinese firms understand that much of the strategic value in acquiring a European firm is the "tacit tech knowhow and management skills embedded in European human capital," not just

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[44] Rongji, "Report on the Outline of the Tenth Five-Year Plan for National Economic and Social Development (2001)."
[45] Meunier, "'Beggars Can't Be Choosers': The European Crisis and Chinese Foreign Direct Investment in the European Union."
[46] Knoerich and Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe."
[47] Derek Scissors, "China Global Investment Tracker," American Enterprise Institute, 2019, https://www.aei.org/china-global-investment-tracker/; Knoerich and Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe."

the tangible assets themselves.[48] As such, Chinese firms often approach post-acquisition with a light-touch strategy, tending not to completely reorganize units or integrate European firms into the parent company. This technique stands in stark contrast with the approach of many other large Western firms who take a more hands-on approach post-acquisition.[49] The results of this acquisition strategy is evident in the pattern of Chinese OFDI in the EU; the vast majority of Chinese OFDI in the EU takes the form of acquisitions whereas greenfield investment has consistently accounted for under 5% of yearly OFDI.[50]

Chinese firms have also looked to capitalize on the international visibility of many major European brands as a way to build-up the popularity of Chinese brands. Despite the growth of many major Chinese brands in recent years, increasing international brand recognition, especially in consumer goods, still remains an area for improvement. Once again, the Chinese strategy has been to build off the brand reputation of respected European firms rather than develop brand reputation from scratch.[51] The acquisition of Volvo, as well as apparel companies Robert Clergerie and Aquascutum are notable examples.[52] Acquiring reputable European brands further benefits Chinese firms by enhancing their reputation in home markets, even introducing previously unpopular or unavailable European products to Chinese consumers.[53] Such has been the case with French wine. Chinese investors have sunk huge sums into buying

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[48] Knoerich and Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe."
[49] Ibid.
[50] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."
[51] Meunier, "'Beggars Can't Be Choosers': The European Crisis and Chinese Foreign Direct Investment in the European Union."
[52] Ibid.
[53] Knoerich and Miedtank, "The Idiosyncratic Nature of Chinese Foreign Direct Investment in Europe."

up vineyards in Bordeaux and Burgundy, driving up demand back home in the process.[54] In essence, European brand acquisition provides a twofold bump in popularity for Chinese brands. Acquisitions of distinguished European brands provides a boost to Chinese firms abroad, especially those in the fashion or luxury goods sectors, by signaling their legitimacy and quality as international brands to Western consumers. Domestically, the impact of European brand acquisition is even greater, as it allows Chinese firms to introduce new, high quality goods to an increasingly affluent Chinese market.

The concentration of high-tech firms and world-renowned brands in Western and Northern Europe may help explain why Chinese OFDI has been so focused in these regions. Firms are asset-seeking in the regions with the highest concentration of desired assets. But Chinese investment dynamics in CEE countries follow slightly different motives, and may fall more in line with traditional market-seeking behaviors. Though as previously mentioned, Chinese OFDI in CEE countries has been meager, China sees strategic investment opportunities in the region. First, Chinese firms see insertion into CEE markets as a way to gain access to the whole EU market, as well as the markets of EFTA member states. Perhaps more important is the fact that many CEE countries offer high-skill labor at lower cost than other Western and Northern European countries, making the establishment of in-country manufacturing facilities in the CEE region an attractive option.[55] This is consistent with the observed characteristics of Chinese OFDI in the region. Greenfield investment constitutes a larger share of Chinese OFDI in

[54] Adam Nossiter, "As Chinese Buy French Vineyards, Names Like Château Imperial Rabbit Rattle Purists," *The New York Times*, April 6, 2019, https://www.nytimes.com/2019/04/06/world/europe/france-china-wine.html.
[55] Szunomár and McCaleb, "Chinese and Other East Asian Foreign Direct Investment in Central and Eastern Europe: Motives, Location Choices and Employment Approaches."

the CEE countries than elsewhere in the EU, in large part because Chinese firms have built manufacturing facilities in the region.[56] Furthermore, Chinese firms see the establishment of production facilities in the CEE region as a way to avoid EU import barriers, and smooth over frustrations that accompany large trade imbalances.[57]

While some of the aforementioned motivations can help account for Chinese predilections for investment in certain EU regions, they do little to explain variation in country-level investment patterns. For example, Chinese OFDI in the CEE countries has been heavily concentrated in Visegrad countries (Hungary and Poland in particular), despite the fact that labor costs and corporate tax rates are lower in Romania and Bulgaria. Moreover, the countries in the most dire financial straits following the GFC, who offered up the lion's share of "bargain basement" deals, did not receive the most Chinese OFDI. In fact, the state of each European economy was not a good indicator of Chinese investment volume and Chinese firms often did not acquire European assets at bargain prices.[58] To better discern country-specific investment motivations, it seems that an understanding of bilateral relations between China and EU countries is fundamental. Beyond traditional domestic factors, such as quality of institutions and openness to investment, research indicates that there is evidence of a "strong link between the intensity of the two-way investment relationship between a member state and China and the propensity of Chinese firms to invest in the EU."[59] In other words, member states that have

[56] Clegg and Voss, "Chinese Overseas Direct Investment in the European Union."
[57] Ibid.
[58] Meunier, "'Beggars Can't Be Choosers': The European Crisis and Chinese Foreign Direct Investment in the European Union."
[59] Clegg and Voss, "Chinese Overseas Direct Investment in the European Union." pg. 24

cultivated an economic relationship with China are most likely to be the beneficiaries of Chinese OFDI.

The Role of SOEs

As previously noted, there is a distinction between Chinese OFDI originating from SOEs and private firms. The majority of Chinese OFDI in the EU since the turn of the millennium has originated from SOEs, though their share has significantly decreased in the past five years. The dominance of SOEs as sources of Chinese OFDI into the EU is unsurprising; SOEs have, until recently, enjoyed an extremely privileged position in the Chinese economy. In fact, the initial years of China's "go global" policy were aimed specifically at promoting SOE expansion abroad. This is in part due to the fact that China's original commercial expansion policies focused primarily on key strategic industries such as natural resource extraction, energy, and telecommunications – sectors in which many Chinese SOEs were uniquely positioned to take advantage.[60] Indeed, SOEs continue to operate monopolies in many of these sectors. For example, the two largest Chinese enterprises are Sinopec and Chinese National Petroleum Corporation (CNPC), both of which are state-owned oil companies. Private firms find it impossible to compete with state-supported conglomerates, and in many cases were explicitly prohibited from competing with SOEs in strategic sectors, which limited possibilities for international expansion in the early 2000s.

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[60] David Shambaugh, *China Goes Global : The Partial Power* (New York: Oxford University Press, 2013), http://web.a.ebscohost.com.ccl.idm.oclc.org/ehost/ebookviewer/ebook?sid=e2f1f470-efeb-4d31-9571-ed6d0c169da9%40sessionmgr4008&vid=0&format=EB.

Chinese policy did not only prioritize SOE-dominated sectors for foreign expansion, but actively supported SOE investment by providing financial support. Private enterprises faced a much more restrictive regulatory environment than their state-owned counterparts, making it difficult to acquire the necessary permits for outward investment.[61] Furthermore, even if private firms did receive permission to invest abroad, they did not receive the same financial favoritism that SOEs enjoyed. SOEs often received loans at artificially low interest rates, were given soft budgets by the state, and were prioritized by national banks.[62] Finally, because most private firms were relatively young and had no international experience, the prospect of investing abroad was daunting. Acquiring a company or launching a greenfield project requires technical expertise and managerial nous, neither of which was in abundant supply in Chinese firms in the early 2000s. Instead, these initial years of "going global", which relied heavily on SOE investment, can be seen as China using country-specific advantages (financial support of SOEs and a favorable regulatory environment) as a way to develop more traditional ownership advantages.[63]

In recent years, SOE investment has begun to account for a smaller share of all Chinese OFDI into the EU. One explanation for this decrease in SOE share of OFDI into the EU is diversification in which sectors are receiving investment. While the 10th five-year plan highlighted SOE-dominated strategic industries for concerted investment efforts, subsequent plans have expanded the scope of Chinese OFDI to a broader set of sectors.[64] Many of these

[61] Huang and Renyong, "Chinese Private Firms' Outward Foreign Direct Investment."
[62] Ibid.
[63] Alan Rugman and Simon Fraser, "Will China's Multinationals Succeed Globally or Regionally?," *European Management Journal* 25, no. 5 (2007): 333–43, https://doi.org/10.1016/j.emj.2007.07.005.
[64] Shambaugh, *China Goes Global: The Partial Power*.

sectors, such as manufacturing, entertainment, and business services, are highly competitive sectors in which private Chinese firms, rather than SOEs, are major players. Moreover, many EU firms are industry leaders in these sectors, making investment in the EU all the more attractive. Simply put, as Beijing has prioritized a broader range of industries for foreign investment, more private Chinese firms have jumped on the opportunity to invest abroad, and in the EU in particular.

The decrease in SOE share of Chinese OFDI into the EU can also be seen as part of a deeper restructuring of the Chinese economy, one in which SOEs do not enjoy the same level privilege that they have since the Deng Xiaoping era. China's growth over the past few decades has been truly remarkable, but President Xi has recognized the limitations of a growth model based on exports, infrastructure investment, and SOE dominance. China's growth has slowed markedly in the past decade as efficiency gains have been hard to come by and debt has saddled the economy. One of Xi's major reform policies has been to put SOEs on a more equal playing field with private firms.[65] While SOEs still hold a privileged status, Xi has worked to eliminate some of the preferential treatment they receive from financial institutions.[66] The same preferential treatment that has allowed SOEs to penetrate international markets, such as soft budgets, artificially low interest rates, and guaranteed monopoly positions, also prevents them from making significant efficiency gains.[67] This last point is particularly important; because most Chinese SOEs face little to no market competition they have little incentive to

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[65] William H. Overholt, *China's Crisis of Success*. (Cambridge: Cambridge University Press, 2017).
[66] Ibid.
[67] Ligang Song, Jidong Yang, and Yongsheng Zhang, "State-Owned Enterprises' Outward Investment and the Structural Reform in China," *China & World Economy* 19, no. 4 (2011): 38–53, https://doi.org/10.1111/j.1749-124X.2011.01249.x.

innovate. Indeed, China has recognized innovation and private entrepreneurship as important drivers of growth for the future, and in turn have looked to eliminate some of the structural disadvantages that private firms face vis-à-vis SOEs.

Investment Cooldown

The decrease in Chinese SOE share of investment in the EU should be seen as a consequence of increased levels of private firm investment, not of decreased levels of SOE investment. It appears that the combination of broader sectoral investment preferences and fewer barriers to OFDI for private firms has succeeded in promoting more private Chinese investment. Despite this sharp increase in the immediate aftermath of the GFC, the past two years have seen an equally sharp decrease in Chinese OFDI into the EU, with experts predicting similarly depressed levels of investment for 2019 and beyond. Once again, the explanation for this trend lies in China's domestic economic policy.

In recent years, China has reimplemented stricter capital controls to curb the amount of money leaving the country. Following years of liberalized outbound capital flows, President Xi Jinping has reined in both private and state-owned investment abroad. This tightening of capital controls is a reactionary measure meant to address a number of macroeconomic goals, including a desire to stabilize the renminbi and counteract a waning current account surplus.[68]

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[68] Maximilian Kärnfelt, "China's Tight Capital Controls Fail to Address Underlying Problems," *Financial Times*, November 10, 2017, https://www.ft.com/content/1d288888-c613-11e7-b2bb-322b2cb39656.

More specifically, it appears that Xi's new capital controls are a direct reaction to what China perceives as capital flight during the years of the outward investment boom.

Though it is hard to discern the true motives for private Chinese OFDI, according to a Baker McKenzie report, the Chinese government interpreted the upsurge in foreign investment as a desire to move capital out of China due to uncertain prospects for continued Chinese growth.[69] The government has publicly cracked down on private firms such as Dalian Wanda, FOSUN, and the HNA group, telling banks not to finance deals and imploring these firms to invest domestically.[70] This strategy has been met with varying degrees of success. Wang Jianlin – China's richest man and Dalian Wanda's CEO – succumbed to the government's pressure whereas Guo Guangchang, FOSUN's CEO, has continued to aggressively pursue deals throughout Europe.[71] The decline of Chinese OFDI in the EU indicates that pressure from the Chinese government has been successful in reeling in foreign investment overall.

Finally, depressed investment levels in Europe may also be a reaction towards a stricter investment environment across the EU. As will be addressed in the following chapter, EU scrutiny over Chinese OFDI has increased in the past few years and a number of notable deals have been blocked by national authorities. As a Baker McKenzie report once again suggests,

[69] "Chinese FDI into Europe Slumps to Four-Year Low, North America Sees Modest Increase in H1 2019" (Chicago: Baker McKenzie, July 11, 2019), https://www.bakermckenzie.com/en/newsroom/2019/07/chinese-fdi-into-europe-new-low.
[70] Shu Zhang and Matthew Miller, "China Cracks down on Dalian Wanda's Overseas Deals: Sources," Reuters, July 17, 2017, https://www.reuters.com/article/us-china-wanda-idUSKBN1A20ER.
[71] Christine Tan and Doran Lim, "Despite Capital Controls, China's 'Warren Buffett' Says He's Pushing Ahead with Overseas Acquisitions," CNBC, March 29, 2017, https://www.cnbc.com/2017/03/29/despite-capital-controls-chinas-warren-buffett-says-hes-pushing-ahead-with-overseas-acquisitions.html.

trepidation towards new EU FDI regulations likely factors into the dip in Chinese OFDI in the EU.[72]

All of the aforementioned trends in Chinese OFDI can be broadly understood as being economically motivated. The huge increase in Chinese investment and subsequent decrease in the past two years falls in line with policy dictated from Beijing; at first there was a push for loosened capital controls and asset-seeking investment, but as the 2010s wore on and capital was leaving China in abundance, President Xi backtracked and has reintroduced stricter capital controls. SOEs were the vanguards of foreign investment, but the Chinese government has begun to level the playing field with private firms. The reason that the EU has seen such a boom of Chinese OFDI is in part due to the enticing economic opportunities present in the post-GFC landscape, and in part due to the composition of the EU market. The combination of European human capital and managerial knowhow, highly recognizable brands, and advanced technologies meant that the EU was replete with many of the strategic assets Chinese firms were seeking.

The literature on Chinese investment dynamics in the EU makes little mention of political motives for Chinese investment. It should be noted that most economic policy decisions can be considered inherently political; state economic policy has redistributive effects and influences a country's economic development. This is especially true in China, where a system of state capitalism further blurs the line between state development policy and private economic decision-making. However, there is very little discussion of Chinese investment as a tool to increase Chinese political power in academic literature.

[72] "Chinese FDI into Europe Slumps to Four-Year Low, North America Sees Modest Increase in H1 2019."

It is only in recent years, especially with the increased visibility of BRI, that the potential political motivations for Chinese investment in the EU have suffused the China-EU investment discourse. A variety of commentators, ranging from think-tank fellows to journalists of major publications, have expressed concern about China's growing influence in the EU, yet few go beyond questioning whether Chinese investment has strings attached or ulterior motives. For example, a 2018 *Economist* briefing questions how much of China's EU investment can be chalked up to grand strategy ambitions, and a 2019 article from *The Guardian* asked if Europe knows the true price of China's billions.[73] Reports from the ECFR and Czech Association for International Affairs (AMO) considers the link between Chinese investment in CEE counties and increased political influence.[74] And a senior fellow at the Carnegie Endowment, in a testimony before the US House of Representatives, claimed that Beijing was intentionally aiming to sow political divisions within the EU.[75]

Unsurprisingly, official Chinese rhetoric towards OFDI in the EU makes no mention of political motivations and Chinese bureaucrats and scholars alike refute the narrative of Chinese investment being a tool for political gain.[76] With such polarized perceptions of Chinese OFDI in

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[73] "Gaining Wisdom, Marching Forward," *The Economist*, October 6, 2018; Juliet Ferguson, "Europe Needs China's Billions. But Does It Know the Price?," *The Guardian*, November 26, 2019, https://www.theguardian.com/commentisfree/2019/nov/26/europe-china-billions-strings-attached.
[74] Angela Stanzel and Agatha Kratz, "China's Investment in Influence: The Future of 16+1 Cooperation," China Analysis (European Council on Foreign Relations, December 2016), https://www.ecfr.eu/publications/summary/chinas_investment_in_influence_the_future_of_161_cooperation7204; Ivana Karaskova et al., "Central Europe for Sale: The Politics of China's Influence," Policy Paper (AMO, April 2018), AMO_central-europe-for-sale-the-politics-of-chinese-influence-1.pdf.
[75] Philippe Le Corre, "On China's Expanding Influence in Europe and Eurasia," § House of Representatives Foreign Affairs Committee (2019), https://carnegieendowment.org/2019/05/09/on-china-s-expanding-influence-in-europe-and-eurasia-pub-79094.
[76] *See* Li Keqiang, "Embracing Openness and Cooperation for Mutual Benefit," *Handelsblatt*, April 8, 2019, sec. Opinion, https://www.handelsblatt.com/meinung/gastbeitraege/gastkommentar-embracing-openness-and-cooperation-for-mutual-benefit/24193230.html?ticket=ST-35590020-UdzGpNZB3btwHcq9HYlo-ap3; Zuokui Liu,

the EU, it will be very difficult to definitively determine to what extent political machinations have guided Chinese investment strategy in the region. However, the state-directed nature of many Chinese OFDI initiatives as well as the emergence of BRI and the 16+1 cooperation framework, which both aim to improve economic and political relations between China and EU member states, suggests that there are political motivations for investing in the EU.

Regardless of the extent to which political considerations guide Chinese investment in the EU, said investment has taken a fundamentally political dimension across the bloc. EU leaders have come to view Chinese investment as not only an economic policy issue, but a political one too. As such, conversations concerning how best to address the influx of Chinese OFDI have become important agenda items in Brussels over the past decade.

Chapter III – EU Institutional Pushback Against Chinese OFDI

As Chinese FDI into the EU has skyrocketed it has been met with increasing skepticism and trepidation. In the immediate aftermath of the GFC, Chinese OFDI was welcomed with open arms across the bloc. This is was especially true in the debt-saddled Mediterranean economies which were in desperate need of capital infusion to jumpstart economic recovery. However, at an institutional level, the EU has toughened its stance on Chinese foreign investment as it relates to national security, technology transfers, state support, and

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"The '16+1 Cooperation' under the 'Belt and Road' Initiative," in *China's Relations with Central and Eastern Europe: From "Old Comrades" to New Partners*, ed. Weiqing Song (London: Taylor and Francis Group, 2017), 29-47.

unreciprocated market access. In fact, as a direct reaction to perceived Chinese economic assertiveness across the continent and beliefs in an unequal playing field for EU firms vis-à-vis their Chinese competitors, the EU now is in the process of implementing a foreign investment screening mechanism and a bilateral investment treaty (BIT) with Beijing.

Evolving Perceptions of Chinese OFDI

The EU's openness to Chinese OFDI over the past decade is unsurprising given the bloc's level of openness to investment overall. According to the OECD's FDI Regulatory Restrictiveness Index (FDI RRI), many EU countries ranked among the most open in the world in 2010 and continue to be ranked near the top currently.[77] Most EU countries are particularly lenient in regards to pre-establishment investment conditions, such as screening and ownership policies, and are ranked well above both the US and the OECD average in terms of overall restrictiveness. In fact, as their rankings in the FDI RRI suggest, only a handful of EU countries had any sort of FDI screening mechanism in place prior to 2012.[78] The ideological aversion towards investment restrictiveness across the bloc can perhaps be best summed up by Karel De Gucht, who as European Commissioner for Trade in 2012 stated that "European security screening of new investments is neither desirable nor feasible."[79]

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[77] Haiyan Zhang and Daniel Van Den Bulcke, "China's Direct Investment in the European Union: A New Regulatory Challenge?," *Asia Europe Journal* 12, no. 1 (March 1, 2014): 159–77, https://doi.org/10.1007/s10308-014-0383-9; "Foreign Direct Investment Regulatory Restrictiveness Index," OECD, 2019, https://goingdigital.oecd.org/en/indicator/74/.
[78] Sophie Meunier, "Divide and Conquer? China and the Cacophony of Foreign Investment Rules in the EU," *Journal of European Public Policy* 21, no. 7 (2014): 996–1016, https://doi.org/10.1080/13501763.2014.912145.
[79] Karel De Gucht, "EU-China Investment: A Partnership of Equals Bruegel Debate" (Brussels, June 7, 2012).

Chinese investment in the EU following the GFC did not initially challenge the bloc's stance towards unfettered openness to FDI. In fact, to the contrary, the Euro crisis softened political resistance to Chinese investment. Long term concerns over the quantity and destination of Chinese OFDI were trumped by short term economic priorities, such as reeling in unemployment and finding buyers for privatization plans mandated by the International Monetary Fund (IMF).[80] Thus, Chinese investment was courted across the EU, with countries such as Hungary going as far as to offer citizenship by investment.[81] Even France, a country which has traditionally been more cautious towards inward foreign investment, was receptive of Dongfeng's 2014 investment into floundering Peugeot.[82] Though European leaders understood that Chinese FDI in Europe could present possible long term concerns, the short term benefits of Chinese capital for domestic economies took precedence. Once again, Karel De Gucht's reminder, "let us be frank: we need the money," seemed to the capture the collective feeling in a still-recovering Europe.[83]

Despite an EU-wide prioritization of economic recovery, of which an infusion of Chinese capital was an important piece, concerns over the size and scope of Chinese OFDI began gaining traction across the bloc. Though there is a dearth of extensive public opinion data regarding European perceptions of China, a poll commissioned by the BBC in 2011 found that negative

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[80] Sophie Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States," in *China's International Investment Strategy: Bilateral, Regional, and Global Law and Policy,* ed. Julien Chaisse (London: Oxford University Press, 2019), 345-71.
[81] F De Beule and Daniel Van Den Bulck, "Changing Policy Regimes in Outward Foreign Direct Investment: From Control to Promotion," in *Foreign Direct Investment from Emerging Markets. The Challenges Ahead,* ed. Sauvant et al. (New York: Palgrave Macmillan, 2010), 277–305.
[82] Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."
[83] De Gucht, "EU-China Investment: A Partnership of Equals Bruegel Debate."

perceptions of China's economic practices were on the rise in a number of major EU countries.[84] In comparison with a poll from 2005, negative perceptions of China's economic growth have increased by 22 points in France, 10 points in both Germany and Italy, and 7 points in the UK.[85] While most respondents identified unfair trade practices as their primary gripe with China, think-tankers and EU bureaucrats were becoming increasingly concerned with Chinese investment practices. For example, a 2011 European Council on Foreign Relations (ECFR) policy brief entitled "The Scramble for Europe" warned against China's "exploitive" investment practices in post-crisis Europe and called for a more coordinated approach to managing incoming Chinese FDI.[86] In a letter written to EU Commission President José Manuel Barroso, Commissioners for Industry and Entrepreneurship, Antonio Tajani, and the Internal Market, Michel Barnier, voiced similar concerns over the explosion of Chinese (as well as Russian) OFDI. In particular, the two Commissioners implored Barroso to consider a supranational body to vet foreign investment into the bloc as a way to protect critical European technology.[87]

Calls for caution towards Chinese investments in the EU became more prevalent as Chinese firms redoubled their investment efforts and a handful of major Chinese investments fell through. As noted in the chapter on FDI flows, prior to the GFC, Chinese investment into the EU was negligible, and from 2010 to 2016 there has been only one year (2013) in which the quantity of Chinese OFDI into the EU has not increased markedly. The novelty of Chinese

[84] "Rising Concern about China's Increasing Power: Global Poll," GlobeScan, March 27, 2011, https://globescan.com/rising-concern-about-chinas-increasing-power-global-poll/.
[85] Ibid.
[86] François Godement, Jonas Parello-Plesner, and Alice Richard, "The Scramble For Europe," Policy Brief (European Council on Foreign Relations, 2011), https://www.ecfr.eu/page/-/ECFR37_Scramble_For_Europe_AW_v4.pdf.
[87] Sophie Meunier, "Integration by Stealth: How the European Union Gained Competence over Foreign Direct Investment," *JCMS: Journal of Common Market Studies* 55, no. 3 (2017): 593–610, https://doi.org/10.1111/jcms.12528.

investment into the EU as well as the rapidity with which it has grown, is, in and of itself, a source of anxiety for many Europeans.[88] Numerous authors have drawn the comparison between contemporary European fears of Chinese investment with American fears over the explosion of Japanese OFDI in the US in the 1980s[89] or even French concerns over the pervasion of American consumerism in the 1990s.[90]

Yet, critical attitudes toward the influx of Chinese capital are not solely visceral and protectionist reactions to the novelty Chinese OFDI. A number of high-profile, unsuccessful Chinese investments in the EU put Chinese investment practices under the microscope, calling into question the motivations of Chinese firms and their level of entanglement with the Chinese government. For example, in 2010 Tianjin Xinmao withdrew its bid for Dutch fiber optic cable company, Draka, after receiving significant pushback from Dutch parliamentarians who saw the proposed takeover as an attempt to siphon-off key European technology.[91] Competition concerns were raised most notably during Chinese Overseas Engineering Company's (COVEC) unfinished highway project in Poland, in which the SOE was able to win the construction contract with a 30-50% lower bid price than competitors, and a 2012 EU investigation into Huawei and ZTE for receiving unacceptable government subsidies.[92] All of these cases did little

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[88] Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."
[89] *See* Fareed Zakaria, "The New China Scare," *Foreign Affairs*, December 14, 2019; Curtis Milhaupt, "Is the U.S. Ready for FDI from China? Lessons from Japan's Experience in the 1980s," Investing in the United States: A Reference Series for Chinese Investors (New York: Vale Columbia Center, 2008), http://ccsi.columbia.edu/files/2014/01/MilhauptFinalEnglish.pdf; Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."
[90] Richard Kuisel, *The French Way: How France Embraced and Rejected American Values and Power* (Princeton: Princeton University Press, 2011).
[91] Zhang and Van Den Bulcke, "China's Direct Investment in the European Union."
[92] Ibid.

to paint Chinese investment in a positive light and pushed the EU to take a more critical stance toward Chinese investment.

The evolution of the EU's position towards China can be seen most clearly in their official strategy documents regarding China. More specifically, from 2013 to 2019, the EU's rhetoric vis-à-vis China has taken on a tougher and more pragmatic tone. In 2013, the EU and China released the "EU-China 2020 Strategic Agenda for Cooperation," a sixteen page, jointly adopted document which identifies a variety of policy areas for future cooperation, ranging from peace and security to people-to-people exchanges. As would be expected in a jointly adopted document, the tone is quite amicable. There are a number of specific goals, especially in terms of economic policy, that directly address EU concerns with China, yet they are articulated in a hopeful and non-accusatory way. For example, rather than state that China is using shoddy regulatory standards as a pretense for limiting market access for EU goods, the agenda states that both the EU and China "confirm their commitment towards international standardization and notification of any standards-restricting market access."[93]

Though the EU has reaffirmed its support for the policy agenda articulated in the "EU-China 2020 Strategic Agenda for Cooperation," the Commission found it necessary to release a document entitled "Elements for a new EU strategy on China" in 2016. The tone of the strategy document is undoubtedly firmer than the 2013 agenda, with the EU recognizing the importance of putting "its own interests at the forefront in the new relationship" and of the "constructive

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[93] European External Action Service, "EU-China 2020 Strategic Agenda for Cooperation" (European Union, November 23, 2013), https://eeas.europa.eu/sites/eeas/files/20131123.pdf.

management of differences."[94] Moreover, the 2016 strategy document directly calls out many of China's problematic economic practices which were alluded to in the 2013 agenda. In particular, "Elements for a new EU strategy on China" emphasizes China's lack of progress in implementing market-based reforms that open the Chinese economy to foreign firms as well as the lack of "free market principles" that guide Chinese OFDI in the EU.[95] However, the 2016 strategy document falls short of being completely adversarial. The EU firmly highlights areas of concern with the state of the EU-China economic relationship, without presenting the points of contention as unreconcilable differences.

The EU's most recent strategy paper regarding China, released in March of 2019, is its most forceful and pragmatic yet. The document, entitled "EU-China – A strategic outlook," proposes first and foremost a "further EU policy shift towards a more realistic, assertive, and multi-faceted approach."[96] It is the first policy document that explicitly labels China as an "economic competitor" and a "systemic rival promoting alternative modes of governance," and instead of simply imploring China to reform its policies, the document considers ways in which the EU can respond to China's obstinance.[97] For instance, the Commission advocates the adoption of a newly reformed EU public procurement mechanism that "levels the playing field" with China.[98] But most importantly, the Commission's latest China strategy document is suggestive of a marked change in perception toward China. While the EU continues to harp on

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[94] European Commission, "Elements for a New EU Strategy on China" (European Union, June 22, 2016), http://eeas.europa.eu/archives/docs/china/docs/joint_communication_to_the_european_parliament_and_the_council_-_elements_for_a_new_eu_strategy_on_china.pdf.
[95] Ibid.
[96] European Commission, "EU-China - A Strategic Outlook" (European Union, March 12, 2019), https://ec.europa.eu/commission/sites/beta-political/files/communication-eu-china-a-strategic-outlook.pdf.
[97] Ibid.
[98] Ibid.

many of the same policy concerns that have been voiced for over a decade, it seems to conceptualize its relationship, especially its economic relationship, with China in a more realistic way. The EU recognizes that if China has failed to implement a broad set of market-based reforms, which often benefits Chinese domestic industry at the expense of the EU, they are unlikely to change their ways moving forward.

This shift in the Commission's perception towards China's economic policies – from hopeful and patient to more pessimistic and adversarial – has been amplified in the past year. The Federation of German Industries (BDI), in a recent study, contends that "for a long time it looked as if China would move towards the liberal, open-market economies of the West by integrating into the world economy and reshaping its economic system. This theory of convergence is no longer tenable."[99] The BDI's perspective is shared by European leaders such as French President Emmanuel Macron, German Chancellor Angela Merkel, and Austrian Chancellor Sebastian Kurz, who this year decried the EU's naïve reaction to China's economic practices. Macron in particular addressed concerns over Chinese OFDI in the EU, labelling China's rapid acquisition of EU infrastructure as a "strategic error" on the EU's part.[100]

While the growing discontent with China's economic policies, as enumerated in the various EU strategy documents and by certain European leaders, does not center solely around Chinese investment practices, Chinese OFDI in the EU has brought many of the EU's concerns to the forefront. At the most basic level, the EU has begun to realize that the usual benefits of

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[99] Bundesverban der Deutchen, "Partner and Systemic Competitor - How Do We Deal With China's State-Controlled Economy?," Policy Paper (Berlin: BDI, January 2019).
[100] Philip Blenkinsop and Robin Emmot, "EU Leaders Call for End to 'naivety' in Relations with China," Reuters, March 22, 2019, https://www.reuters.com/article/us-eu-china-idUSKCN1R31H3.

foreign investment for the recipient economy may not be materializing. When addressing the issue of Chinese FDI in the EU in 2012, De Gucht reiterated what was thought to be common knowledge in FDI literature: foreign investment would increase trade and economic activity with the country of origin and the recipient economy would gain technological, organizational, and managerial skills.[101] But as noted in the previous chapter, China's motivation for investing in more advanced economies than its own is to acquire technology and managerial knowhow for its own firms. The "reverse flow" phenomenon is true for high-tech sectors, many of which are included in the Chinese government's "Made in China 2025" plan, as well as in less geostrategic areas such as soccer.[102] In the past decade, China has made a huge push to develop its domestic soccer league and turn the country into, in the words of President Xi , a "soccer powerhouse."[103] To help achieve this goal, China has attracted high-profile foreign players to its domestic league and acquired a number of major European clubs, such as one of Italy's most historic and successful clubs, Internazionale.

Fears of Losing Technological Superiority

Chinese FDI in the EU has elicited some of the harshest backlash because of the possibilities for technology transfer. The prospect of Chinese firms acquiring European technology leaders as a way to upgrade its industrial capabilities at Europe's expense is one of

[101] De Gucht, "EU-China Investment: A Partnership of Equals Bruegel Debate."
[102] Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."
[103] Owen Gibson, "The Great Windfall of China: A Football Revolution That May Lead to World Cup," *The Guardian*, February 6, 2016, https://www.theguardian.com/football/blog/2016/feb/06/china-football-revolution-world-cup.

the EU's biggest concerns. The "Made in China 2025" policy has the explicit goal of moving China up the value chain in ten important industry sectors, and acquiring the requisite technology to do so is a key part of the equation. With these motivations in mind, Chinese acquisitions of European tech firms have raised a number of hackles. Predictably, some of the biggest denunciations of Chinese technology transfers have come from Germany, which sees itself as a direct competitor to China in terms of the production and exportation of high-tech goods. For example, Kuka Robotics' takeover by Chinese firm Midea was met with considerable resistance, with many German officials and business leaders seeing it as a hollowing out of Germany's tech industry.[104]

The fear of losing a technological edge in part due to forced technology transfers is a fear grounded in reality. A 2019 survey of 585 European businesses from the European Chamber of Commerce found that more than 20% of respondents and 30% of respondents in high-tech sectors "felt compelled to hand over technology to Chinese business partners."[105] Perhaps of even greater concern is that the percentage of firms who have felt compelled to transfer technology to Chinese partners has doubled from 2017. In some cases, Chinese firms have even reverted to intellectual property (IP) theft to obtain key technologies. IP theft has been a long-held concern of EU member states, as well as the US. Despite Chinese assurances that they are working to fight against IP theft and the fact that specialized courts meant to handle IP theft cases have existed in China since 2014[106] (and tend to rule in favor of foreign

[104] Elizabeth C. Economy, *The Third Revolution: Xi Jinping and the New Chinese State* (Oxford University Press, 2018).
[105] Don Weinland, "European Companies Forced to Hand Tech to China," *Financial Times*, May 20, 2019, https://www.ft.com/content/f2f4dca0-7abc-11e9-81d2-f785092ab560.
[106] Zakaria, "The New China Scare."

firms), EU firms continue to have proprietary secrets stolen. A recent notable example is the theft of IP from Dutch firm ASML, which makes lithography systems that trace the circuitry of semiconductor chips. Documents from a 2018 court case showed that six ASML employees, all with Chinese names, shared secret software process information with ASML's Chinese competitor, XTAL.[107] Unsurprisingly, XTAL's parent company, Dongfang Jingyuan, has close ties with the Chinese Ministry of Science and Technology.[108]

An Unfair Playing Field

Even in cases where technology transfers are not a major concern, EU firms feel aggrieved that government support for Chinese firms is partially responsible for takeovers. While the EU has a stringent competition policy that prohibits member states from aiding or subsidizing private firms except for in very specific conditions, Chinese firms – both SOEs and private firms – often receive state support in their business dealings. This "unfair playing field" has been noted by the EU in its strategy documents regarding China, and also by the BDI, who assert that foreign takeovers by Chinese firms are aided by "low-cost loans from state-owned banks and direct project-based financing through the state budget and state venture capital."[109] The Chinese government has also helped Chinese firms acquire European firms in more dubious ways, such as the near-takeover of semiconductor company Aixtron by Chinese investment

[107] Zak Doffman, "China's Spies Accused Of Stealing EU Tech Secrets, Just As China And EU Agree Stronger Ties," Forbes, April 11, 2019, https://www.forbes.com/sites/zakdoffman/2019/04/11/chinese-spies-accused-of-major-european-ip-theft-just-as-china-and-europe-agree-stronger-ties/.
[108] Ibid.
[109] Bundesverban der Deutchen, "Partner and Systemic Competitor - How Do We Deal With China's State-Controlled Economy?"

fund Fujian Grand Chip. In 2015, Chinese firm Sanan Optoelectrics, which has connections with both Fujian and the Chinese government, cancelled a large order at the last minute, causing Aixtron's stock to crash and opening the door for Fujian to submit a bid to acquire Aixtron.[110] The acquisition fell through only after the German government withdrew its approval of the takeover under US pressure.

Another way in which the EU feels that the playing field is unfair for EU firms is in the lack of reciprocal access to Chinese markets. While the EU has given China nearly unrestricted access to one of the world's largest markets, China has been slow to provide similar levels of market access for EU firms in China. Once again, the EU expected that increased levels of Chinese FDI in the EU would open the door for EU firms to invest in China,[111] but a litany of market-access restrictions are in place for EU firms. Some restrictions are direct, such as simply not allowing foreign firms to penetrate certain sectors, such as fintech. In other cases, market access is restricted in less overt ways, such as by requiring EU firms to launch joint ventures with Chinese counterparts, strict localization requirements, including for data; limiting foreign access to government-funded programs, applying strict and sometimes inconsistent regulatory standards on foreign goods, and a lack of transparency in investment protection.[112]

An area in which the imbalance of market access is particularly acute is the case of procurement policy. Chinese firms are able to bid on public projects throughout the EU (and often do so at a lower price than any EU firm can), yet most public projects in China are only

[110] Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."
[111] De Gucht, "EU-China Investment: A Partnership of Equals Bruegel Debate."
[112] European Commission, "EU-China - A Strategic Outlook."

open to Chinese firms. In fact, China has not signed onto the WTO's Agreement on Government Procurement (GPA), which would otherwise prevent them from discriminating against foreign bidders. As a result, bidding for all of China's mega-projects is administered by the National Development and Research Committee and awarded exclusively to Chinese firms.[113]

Security Concerns

Finally, Chinese OFDI has presented EU leaders with concerns over national and supranational security. In recent years, the EU has begun to recognize that China has superpower ambitions, and many of those ambitions are antithetical to the EU's interests. The EU and China are by no means enemies, but nor are they security allies. Historically, the US and the EU are unaccustomed to receiving significant amounts of investment from non-security allies; indeed, neither the US nor the EU received any investment, let alone traded with, the Soviet Union during the Cold War.[114] The murky nature of the Chinese government's involvement with Chinese firms only heightens security concerns. It is hard to for the EU to gauge whether investments serve purely commercial interests or if there are ulterior motives. As previously discussed, these concerns have been manifested in the cases of sensitive technology, such as semiconductors or dual-use technologies. For example, Huawei has faced consistent scrutiny from the EU, most recently in a bloc-wide 5G security assessment released

[113] Godement, Parello-Plesner, and Richard, "The Scramble For Europe."
[114] Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."

in October 2019.[115] Or, in 2018, the German government blocked two potential Chinese investments on national security grounds. The Yantai Tahai Group was prevented from taking over an advanced manufacturing company, Leifeld Metal Spinning AG, and China's State Grid Corporation was blocked from acquiring a 20% share in 50Hertz, a provider of high-voltage transmission systems.[116]

The security dimension of Chinese investments also encompasses critical infrastructure. Though Chinese investment in European infrastructure, such as the Port of Piraeus or a large portion of Portugal's power grid, was welcomed in the aftermath of the GFC, on an institutional level the EU has grown warier. Notably, former British Prime Minister Theresa May reviewed the proposed takeover of Hinkley Point nuclear power plant in 2016 by a French consortium and the Chinese SOE General Nuclear Power Group (CGN). Though the deal eventually went through, May was considering the security implications of letting China have control over UK power production.[117] Concerns with Chinese control of critical infrastructure were only heightened with the arrival of China's Belt and Road initiative in the EU. Though the amount of BRI investment in the EU is meager in comparison with BRI investment in Asia and Africa, it is still viewed by the EU as a security challenge. In 2018, the EU went as far as to release its own strategy document on improving Europe-Asia connectivity as a way to counter China's BRI

[115] NIS Cooperation Group, "EU Coordinated Risk Assessment of the Cybersecurity of 5G Networks" (Brussels: European Union, October 9, 2019).
[116] Arne Delfs, "Germany Toughens Stance and Blocks China Deal," Bloomberg.com, August 1, 2018, https://www.bloomberg.com/news/articles/2018-08-01/germany-said-to-block-company-purchase-by-chinese-for-first-time.
[117] Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."

presence throughout the EU. The EU document makes no mention of BRI, and presents itself as a "sustainable, comprehensive, and rules-based" alternative to the Chinese model.[118]

Toward a Bilateral Investment Treaty

The EU's new Euro-Asia connectivity strategy is just one of the ways in which the EU is trying to substantively push back on Chinese FDI, and it remains to be seen what impact it will have on the level of BRI investment in the EU. The EU has been responding to its various concerns with Chinese investment in two other major ways: pursuing a BIT and implementing a foreign investment screening mechanism. The competence of foreign investment policy was transferred from the national to the supranational level by the 2009 Lisbon Treaty, and over the past decade the EU has taken more control over the bloc's overall investment policies. Though the specifics of what the term "foreign direct investment" means are not fleshed out in the Lisbon Treaty, the EU has taken the initiative to negotiate a Comprehensive Agreement on Investment (CAI) with China as well as, more recently, implement a bloc-wide framework for screening foreign investments.

CAI negotiations, which aim to adopt a BIT between the EU and China have been ongoing since 2013. The CAI was referenced in the "EU-China 2020 Strategic Agenda for Cooperation," and has been a key agenda matter at the annual EU-China summits. The overarching goal of the CAI, from an EU perspective, is to level the playing field between EU

[118] European Commission, "Connecting Europe and Asia - Building Blocks for an EU Strategy" (European Union, September 19, 2018), https://eeas.europa.eu/sites/eeas/files/joint_communication_-_connecting_europe_and_asia_-_building_blocks_for_an_eu_strategy_2018-09-19.pdf.

firms and their Chinese counterparts by bringing Chinese policy closer in line with the tenets of the Western, market-based economic order. The main priorities of the CAI, which have also unsurprisingly been the biggest stumbling blocks in reaching an agreement, are to further open up the Chinese market to European FDI and to protect investments.[119] As previously discussed, China employs a variety of levers to limit market access for foreign firms, all of which the EU is keen to address as part of the CAI. EU leaders have voiced their frustration with the slow progress of negotiations, which they hope to conclude by 2020, but see ongoing dialogue with China on economic issues as a way to sustain liberalization pressures.

The even greater of benefit of conducting a single BIT negotiation between the EU and China is that it presents a unified voice to China. Prior to 2013, each EU member state had to negotiate a BIT with China individually, which placed the power squarely in China's hands.[120] China could use its greater economic leverage to force concessions out of EU member states, especially some of the bloc's smaller members. Moreover, the lack of a unified policy vis-à-vis inbound Chinese FDI means that China can play member states off one another, needing investment access to only a single member state to have access to the whole EU market.[121] But by negotiating as an entire bloc, the EU is able to eliminate some of China's bargaining leverage. This has been an EU focus for a number of years, and was bluntly stated in their 2016 China strategy document:

> "The EU must project a strong, clear and unified voice in its approach to China. When Member States conduct their bilateral relations with China… they should cooperate with the Commission, the EEAS and other Member States to help ensure that aspects

[119] Meunier, "Divide and Conquer? China and the Cacophony of Foreign Investment Rules in the EU."
[120] All EU member states except Ireland currently have BITs in place with China
[121] Meunier, "Divide and Conquer? China and the Cacophony of Foreign Investment Rules in the EU."

> relevant to the EU are in line with EU law, rules and policies, and that the overall outcome is beneficial for the EU as a whole."[122]

What makes an EU-led BIT negotiation with China particularly powerful is that internal interests are aligned quite uniformly in regards to OFDI policy; the desire to gain greater market access in China and compete on a more equal playing field with Chinese firms is shared across the bloc.

FDI Screening

If CAI negotiations represent an attempt to bolster the EU's OFDI in the direction of China, the newly announced investment screening mechanism directly addresses concerns with the nature of inward investment from China. Calls for an EU-wide foreign investment screening mechanism date back to 2011, when Commissioners Tajani and Barnier brought the idea forward in a letter. But it was not until 2017 that the idea of a supranational screening mechanism gained enough political momentum for then Commission President Juncker to propose a framework. Juncker's proposal gained institutional consensus quickly, and in April 2019, the European Parliament passed the regulation establishing the new FDI screening framework. While the adoption of the new framework is once again a positive step in presenting a unified EU voice to China, its effectiveness as a tool to protect against Chinese OFDI detrimental to EU interests remains to be seen.

[122] European Commission, "Elements for a New EU Strategy on China."

Unlike the Committee on Foreign Investment in the United States (CFIUS), which is a committee given the powers to review and potentially block FDI in the US for national security reasons, the EU's FDI screening framework has no enforcement capabilities. Rather, it is a framework for increased cooperation and coordination whereby EU states can share and request information regarding specific foreign investments that potentially impact on their national security and public order.[123] Additionally, the new regulation allows the Commission to voice opinions on foreign investments[124] affecting multiple EU member states or foreign investments that impact the EU as a whole, though these opinions are non-binding for the member state who is the beneficiary of the investment.[125] When giving its opinion on the quality of the foreign investment, the Commission is to pay particular attention to deals in sectors such as critical infrastructure, critical technologies and dual-use items, supply of critical inputs, access to sensitive information, and media. Finally, when considering whether or not a deal is "likely to affect security or public order," the Commission will primarily take into account three criteria: whether the foreign investor is directly or indirectly controlled by the government of a third state, whether the foreign investor has previously been involved in activities affecting security or public order, and whether there is a "serious risk" that the foreign investor engages in illegal activity.[126]

Though the regulation explicitly states a stance of non-discrimination against the investment's country of origin, it is clear that many of the framework's provisions address the

[123] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."
[124] The regulation only allows M&A investments to be reviewed, not greenfield or portfolio investments
[125] European Parliament and the Council of the European Union, "Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 Establishing a Framework for the Screening of Foreign Direct Investments into the Union" (2019), https://eur-lex.europa.eu/eli/reg/2019/452/oj.
[126] European Parliament and the Council of the European Union.

core characteristics of Chinese OFDI in the EU. SOEs still account for a significant share of Chinese OFDI in the EU, and a number of Chinese firms have already faced lawsuits over IP theft and other illicit business activities. In fact, analysis from the Rhodium Group found that if the regulation's review criteria had been applied to China's 2018 OFDI in the EU, approximately 83% of investments could have fallen under Commission scrutiny.[127] It is uncertainwhat opinion the Commission would release regarding any specific investment or if member states would comply with the opinion, but clearly the new framework will place Chinese OFDI more squarely under the microscope.

What is interesting to note is that prior to the new pan-EU investment screening framework, the EU did have the capacity to review foreign investments in specific cases. The European Programme for Critical Infrastructure Protection (EPCIP), which was implemented in 2006, allowed the EU to review foreign investments into critical infrastructure on national security grounds, and the EU Merger Regulation (EUMR), which was reformed in 2004 as part of EU competition law, allows the EU to block anti-competitive M&As.[128] However, neither the EPCIP nor the EUMR were often used to block any FDI into the EU, let alone Chinese FDI. The EUMR has been called upon to review potential investments quite frequently, but Chinese firms have seldom been ruled against. In fact, in 2011, five deals involving Chinese SOEs[129] looking to acquire major European firms were reviewed under the EUMR framework, and all five rulings went in the favor of the Chinese SOEs.[130]

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[127] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."
[128] Meunier, "Divide and Conquer? China and the Cacophony of Foreign Investment Rules in the EU."
[129] The SOEs were: China National Bluestar of ChemChina, Huaneng, Sinochem, China National Agrochemical Corporation, and Petrochina
[130] Zhang and Van Den Bulcke, "China's Direct Investment in the European Union."

The EPCIP has seldom been used as a framework for reviewing critical infrastructure investments, in part because the European Court of Justice (ECJ) has tended to rule against claims filed under the EPCIP, interpreting national security narrowly so as to avoid economic protectionism.[131] The ECJ's stance has been echoed by others, most notably Commissioner De Gucht, who in 2012 insisted that "we cannot accept – in Europe or elsewhere – that national security concerns are used as a false pretense to justify the protection of vested economic interests."[132]

The new foreign investment screening framework represents a major step forward for the EU in regards to confronting Chinese OFDI, but it does not increase the EU's capacity to block investments at an institutional level. If anything, the new framework is emblematic of the EU's changing perception of Chinese OFDI. The EU began the decade encouraging Chinese OFDI and denouncing any form of economic protectionism, but has recognized the naivety of that position and recently gone as far as to implement a screening mechanism with a broad remit. The screening mechanism, as well as the CAI, are examples of how the increase in Chinese OFDI in the EU have had a centripetal effect[133] on the EU; the EU has recognized that Chinese OFDI poses unique challenges that are best confronted at a supranational level.

[131] Ibid.
[132] De Gucht, "EU-China Investment: A Partnership of Equals Bruegel Debate."
[133] Meunier, "Divide and Conquer? China and the Cacophony of Foreign Investment Rules in the EU."

Chapter IV – Economic Cleavages in the EU

The explosion of Chinese OFDI into the EU has pushed the bloc to pursue a unified approach toward Beijing, one that leverages the power of all 27 member states to address concerns over Chinese investment practices. However, despite visibly toughening its stance toward China and successfully adopting a foreign investment screening framework, the EU is not completely unified in its China strategy. Chinese OFDI into the EU has actually sowed a number of divisions within the bloc as member states grapple with how to balance apprehensions over Chinese investment practices with the tangible benefits of Chinese capital. In fact, Chinese OFDI has exacerbated a number of pre-existing economic cleavages between member states while also creating new ones. These cleavages, in turn, have undermined the EU's official position on a number of China-related policies, such as investment screening and response to BRI projects in Europe.

The economic divisions that Chinese OFDI has inflamed in recent years are divisions that have underpinned EU economic relations for many decades. In essence, these divisions boil down to the allocation of funding between the EU's larger, more prosperous member states and the smaller, less developed member states on the bloc's periphery. For years, EU funding has been the primary source of "foreign" capital for these less developed member states, but as China has established itself as an alternative source of capital – and one that does not attach the same types of political conditionalities to its funding – the economic dynamics within the EU are shifting.

The Roots of the EU's Economic Cleavages

It is important to recognize that economic divisions between EU member states have been points of contention well before the recent influx of Chinese capital. At its most fundamental level, the EU has been first and foremost an economic union[134] with the goal of integrating the European economies. In fact, the promise of upwards economic convergence has often provided the impetus for many countries to pursue EU accession. But with the integration of national economies into a single market and monetary union have come many challenges, and the distribution of funding between member states has often sparked thorny debate. For example, the allocation of Common Agricultural Policy (CAP) funding has dominated the agenda at many Intergovernmental Conferences and the "UK rebate" has remained, until recently, a source of ire across the bloc.

Beginning with the Mediterranean expansion in the 1980s, the question of structural funds has been a marquee agenda item for many of the EU's smaller and less economically developed member states. The EU has a number of funds meant to smooth out economic and social imbalances between member states and even between specific regions within member states, most notably the European Regional Development Fund (ERDF) and the Cohesion Fund. Many aspiring member states have recognized these funds as an invaluable source of capital to jumpstart an underdeveloped national economy, and thus a motivation for pursuing accession. Indeed, Greece, Spain, and Portugal were able to successfully negotiate for the creation of a cohesion policy as part of their accession agreements, and structural and cohesion funding was

[134] The EU was known as the European Economic Community (EEC) from 1957 until 1993

increased to nearly €235bn from 2000-2006 to support the accession of many CEE countries and Malta as part of the EU's eastern expansion.[135]

The EU's structural and cohesion funds, while an important piece of fostering regional integration, have also created a number of points of tension between member states – tensions that have only sharpened as Chinese capital becomes part of the equation. On the one side, member states have jockeyed with one another to receive a larger share of structural funding. This was true during negotiations for the 2004 eastern expansion, when Greece, Spain, and Portugal were hesitant to support the accession of the CEE countries out of fear of seeing some of their own funding diverted.[136] Competition over fund allocation is still prominent today too. As the money in the structural and cohesion funds has increased from around €64bn in the 1988-1992 Multiannual Financial Framework (MFF) to over €350bn in the 2014-2020 MFF, regional and national lobbying offices in Brussels have proliferated.[137] Furthermore, EU funding accounts for over 2% of the national budgets of eight EU member states – Greece, Estonia, Latvia, Lithuania, Poland, Romania, Bulgaria, and Hungary – meaning that even small increases or decreases in fund allocation can have significant impacts on domestic spending in those countries.[138] In essence, the tug-of-war over access to EU transfer payments demonstrates how hungry many smaller member states are for any extra investment they can get.

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[135] European Commission, "History of the Policy," 2019, https://ec.europa.eu/regional_policy/en/policy/what/history/.

[136] Grazyna Bernatowicz, "Spain, Portugal and Greece and European Union Enlargement," *Polish Quarterly of International Affairs* 7, no. 2 (1998): 41–54.

[137] Andres Rodriguez-Pose and Julie Courty, "Regional Lobbying and Structural Funds: Do Regional Representation Offices in Brussels Deliver?," *Regional & Federal Studies* 28, no. 2 (March 15, 2018): 199–229, https://doi.org/10.1080/13597566.2018.1441828.

[138] Tamara Kovacevic, "EU Budget: Who Pays Most in and Who Gets Most Back?," BBC News, May 28, 2019, https://www.bbc.com/news/uk-politics-48256318.

While competition between many of the smaller and less developed EU economies has been noteworthy, it has in many ways been overshadowed by the divide between net contributors and net recipients of EU funds. As part of the 2014-2020 MFF, only ten member states were net contributors to the EU budget[139], with Germany leading the way with a €12.8bn net contribution.[140] Unsurprisingly, many of the countries who are consistently net contributors to the EU budget have pushed for reducing their contributions whereas net recipients argue that increased levels of spending are needed to achieve greater convergence.

This cleavage between the larger more developed economies and the smaller less developed economies has been especially pronounced during recent negotiations for the 2021-2027 MFF. To address the €13bn funding gap created by the UK's departure from the EU, leaders from the so-called "frugal five" countries – the Netherlands, Sweden, Denmark, Austria, and Germany – have advocated for spending cuts to the structural and cohesion funds.[141] Their proposal was met with harsh opposition by the 16 "friends of cohesion," a group of the EU's Southern and Eastern member states, all of whom are net recipients of EU structural and cohesion funds.[142] While the net contributors see the cut in structural funding as a necessary step towards pursuing new programs and accounting for the UK's departure, the friends of cohesion see the move as unacceptable.[143] Hungarian Prime Minister Viktor Orbán even went

[139] The ten countries are, in order of net contribution: Germany, the UK, France, Italy, the Netherlands, Sweden, Austria, Denmark, Ireland, and Finland
[140] Kovacevic, "EU Budget."
[141] Their proposal aimed to cut Cohesion funding and CAP funding by 7% and 5% respectively and limit EU contributions to 1% of GNI
[142] Eszter Zalan, "'Cohesion' Countries Fight Back to Defend EU Funds," EUobserver, November 6, 2019, https://euobserver.com/economic/146530.
[143] Government of the Czech Republic, "Friends of Cohesion: Joint Declaration on the Multiannual Financial Framework 2021–2027," November 11, 2019, https://www.vlada.cz/en/media-centrum/aktualne/friends-of-cohesion-joint-declaration-on-the-multiannual-financial-framework-2021-2027-177497/.

as far as to claim that as a result of the new proposal “the poorer will get less and the richer will get more,” further fanning the flames between the two blocs of member states.[144]

The division between net contributors and net recipients of EU funds is not the only enduring economic fault line cutting through the bloc. A related cleavage, the North-South cleavage, continues to pose challenges to the EU’s economic unity. Perhaps these two cleavages should not be considered completely separate, as there is a significant amount of overlap between Northern, contributor member states, such as the frugal five and France, and Southern, recipient member states, such as Greece, Portugal, Spain, Malta, and Cyprus. However, the specific dynamics of the North-South cleavage have become especially pronounced as a result of the eurozone crisis.

Though essentially the whole EU suffered as a result of the crisis, many of the Mediterranean countries were hit particularly hard. By late 2011, it became clear that Portugal and Greece would need bailouts and the Troika – the Commission, European Central Bank, and the IMF – deliberated on how best to do so. The crisis pit creditors against debtors and played into long-held stereotypes regarding the economic practices of the North and the South. Specifically, the Mediterranean countries, and Greece in particular, were blamed for being fiscally profligate and poorly governed by both their creditors to the north and throughout the media.[145] On the other hand, the North, and Germany in particular, was characterized as the iron-fisted overlord of austerity and unnecessary conditionalities. From the Southern European perspective, Germany was primarily concerned with recouping its loans and was reluctant to

[144] *Quoted in*: Zalan, “‘Cohesion’ Countries Fight Back to Defend EU Funds.”
[145] Mai’a K. Davis Cross and Xinru Ma, “EU Crises and Integrational Panic: The Role of the Media,” *Journal of European Public Policy* 22, no. 8 (September 14, 2015): 1053–70, https://doi.org/10.1080/13501763.2014.984748.

help its struggling Mediterranean neighbors.[146] As is usually the case, the truth lies somewhere between, yet bitterness remains.

Chinese OFDI in the EU has done little to quell any of the aforementioned economic tensions across the bloc. Indeed, it is becoming clear that Chinese investment is actually deepening cleavages between the more prosperous net contributors and those to their east and south. The boom of Chinese investment has come precisely when the EU's capacity for and prioritization of investment in its less developed peripheral regions has reached a nadir. Despite the fact that the volume of Chinese OFDI in the Mediterranean and CEE is dwarfed by the volume of structural and cohesion funds flowing to these regions, the perception of an EU reluctant to help its smaller member states contrasts poorly with the sudden influx of Chinese capital. As a result, it appears that a number of EU member states are beginning to view Chinese investment as an attractive alternative, or at the very least a welcome complement, to transfer payments from the EU.

With regards to CEE countries, where the opposition to reducing CAP and cohesion funding in the next MFF have been most emphatic, the impact of Chinese OFDI has been particularly notable. Greenfield investment has been steadily increasing in the region and a report from the Mercator Institute and the Global Public Policy Institute even goes as far to claim that China has targeted the region with economic cooperation agreements that "promise to compensate for the EU's allegedly limited ability to support development in the region after

[146] Ibid.

the crisis."[147] Whether undermining the EU's competence over regional development in CEE countries is a Chinese policy goal or not, Chinese OFDI has generally been welcomed with open arms throughout the region. Slovak Deputy Prime Minister Richard Rasi, recently stated that he sees Chinese investment as a key driver of the country's growth,[148] and Czech President Milos Zeman deemed his country "an unsinkable aircraft carrier of Chinese investment expansion" in Europe.[149] Most strikingly, Hungarian Prime Minister Viktor Orbán has explicitly leveraged Chinese investment to try to prevent the EU from decreasing structural funds sent to Hungary, by declaring that "Central Europe needs capital to build new roads and pipelines. If the EU is unable to provide enough capital, we will just collect it in China."[150] What is especially revealing about Orbán's statement is that it shows a prevailing conceptualization in Hungary of the EU as the "other." Despite the fact that Hungary is a constituent part of the EU, Orbán does not appear to view China and the EU differently as sources of capital.

Chinese investment has not only exacerbated economic divisions between the EU's net creditor member states and CEE countries, but also with many Mediterranean countries. The dynamics are once again similar, with China acting as a newfound source of capital for countries in which capital is in short supply. However, China perhaps occupies an even more delicate position in the countries hit hardest by the eurozone crisis. When the Troika imposed austerity

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[147] Thorsten Benner et al., "Authoritarian Advance: Responding to China's Growing Political Influence in Europe" (Mercator Institute for China Studies & Global Public Policy Institute, February 2018), https://www.merics.org/sites/default/files/2018-02/GPPi_MERICS_Authoritarian_Advance_2018_1.pdf.
[148] Yang Kunyi, "China's Investment in Slovakia Expects Huge Rise: Deputy PM," Global Times, November 26, 2019, http://www.globaltimes.cn/content/1171256.shtml.
[149] *Quoted in*: David Barboza, Marc Santora, and Alexandra Stevenson, "China Seeks Influence in Europe, One Business Deal at a Time," *The New York Times*, August 12, 2018, https://www.nytimes.com/2018/08/12/business/china-influence-europe-czech-republic.html.
[150] *Quoted in*: Benner et al., "Authoritarian Advance."

and mandated privatization plans in Greece and Portugal as conditions for their respective bailouts, it was China that bought both sovereign debt and previously public assets.[151] In fact, in the case of Portugal, China is estimated to have bought 45% of all assets put for privatization under the Economic Adjustment Program.[152] Recently, Germany's outspokenly critical stance toward Chinese investment throughout the EU has done little to repair relations with Greece and Portugal, who cannot help but note the hypocrisy in the German position; by requiring Greece and Portugal to sell-off public assets and by refusing to increase transfer payments to these crisis-stricken countries, Germany pushed Greece and Portugal into Chinese arms.[153] As the secretary-general of the Portugal-China Chamber of Commerce and Industry, Sérgio Martins Alves, tritely conceded, "we just sold to the guys offering the most money – and evidently they were always Chinese in that period."[154]

In any case, the arrival of Chinese capital *en masse* in the Mediterranean has aggravated the already rocky relation between North and South, reinforcing each region's respective stereotypes of one another. The North sees the Mediterranean's openness to Chinese investment as risky and shortsighted – signs of poor long-term economic planning. On the other hand, the arrival of Chinese capital on Mediterranean shores when little was coming from the North has worsened the North's harsh, inflexible; and above all else, self-interested, image.

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[151] Michael Martina and Andreas Rinke, "China Says Willing to Buy EU Bonds amid Worsening Crisis," Reuters, August 30, 2012, https://www.reuters.com/article/us-china-europe-idUSBRE87T0BY20120830.
[152] Meunier, "Beware of Chinese Bearing Gifts: Why China's Direct Investment Poses Political Challenges in Europe and the United States."
[153] Laurens Cerulus and Jakob Hanke, "Enter the Dragon: Chinese Investment in Crisis-Hit Countries Gives Beijing Influence at the European Union's Top Table," POLITICO, October 4, 2017, https://www.politico.eu/article/china-and-the-troika-portugal-foreign-investment-screening-takeovers-europe/.
[154] *Quoted in*: Cerulus and Hanke.

China's Influence Over Foreign Investment Review

Interestingly, Chinese OFDI has gone beyond simply reinforcing pre-existing economic divides across the EU and has created many of its own unique points of conflict. For instance, the divide between national interest and local concern is visible all across the bloc. Whereas national governments may be wary of investment, municipalities and even private industry who can stand to benefit from Chinese investment do not feel the same way.[155] Though concerns over the level and type of Chinese OFDI in the EU are in some cases justified, the undeniable benefits of Chinese investment for many cities and companies makes the political calculus for national leaders more difficult. Similarly, the rise of Chinese OFDI in the EU has also reshaped some of the economic cleavages between member states. When it comes to foreign investment screening, a division has emerged between member states highly concerned with the security implications of Chinese investment and those whose thirst for foreign investment trumps security concerns.

Germany and France are the member states who have voiced their qualms with Chinese investment practices most resoundingly and who have led the charge at the EU level for a firmer approach to China. In many ways, they have begun to question whether Chinese OFDI represents a "Faustian bargain," fearing that the short-term benefits of increased investment

[155] The case of Duisburg, Germany and Marseille, France are great examples. Though both national governments have been outspokenly suspicious of Chinese OFDI, Duisburg and Marseille have both benefitted from Chinese initiatives to turn the cities into Europe's largest inland port and the Mediterranean's largest wholesale trade center, respectively. This dynamic has been repeated in the case of struggling companies eager for a new owner or investment. While national governments may balk at the idea of Chinese takeovers, managers and employees tend to be happy with the results.

are outweighed by potential drawbacks down the line.[156] As large, prosperous economies, Germany and France are not as hungry for FDI to drive growth as many other smaller EU member states are and can thus afford to be pickier with what foreign investments they allow on their soil. Plus, because Chinese firms have often acquired, or attempted to acquire, German and French firms in sectors deemed critical to the national interest, the perceived value of Chinese OFDI has not been unequivocally positive. The specific fears of having technology siphoned off by China, and losing their place as leaders in the production of high-quality, high-tech goods have also been filtered through a Western geopolitical lens.[157] As their increasingly adversarial rhetoric vis-à-vis China suggests, German and French leaders may equate the explosion of Chinese OFDI in the EU with the rise of China more generally.[158] As G8 members and world leaders, Germany and France are perhaps more prone to Western anxieties of being eclipsed by China, and the sudden insertion of Chinese capital into the heart of Europe does little to alleviate these fears.

While Germany and France have been calling for less naivety toward Chinese OFDI, some of their traditional economic allies have expressed diverging opinions. Countries such as the Netherlands, Sweden, Denmark, and Finland, who are often referred to colloquially as the "ideological free traders," have increasingly sided with Mediterranean and CEE member states on the issue of foreign investment screening.[159] On one level it might appear logical that the Nordics and the Netherlands – who are some of the world's most open countries to foreign

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[156] Sophie Meunier, "A Faustian Bargain or Just a Good Bargain? Chinese Foreign Direct Investment and Politics in Europe," *Asia Europe Journal* 12, no. 1 (March 1, 2014): 143–58, https://doi.org/10.1007/s10308-014-0382-x.
[157] "Foreign Investment Screening and the China Factor," Rasmussen Global, accessed December 16, 2019, https://rasmussenglobal.com/media/foreign-investment-screening-china-factor-memo.
[158] Meunier, "A Faustian Bargain or Just a Good Bargain?"
[159] "Foreign Investment Screening and the China Factor."

investment according to the OECD's FDI RRI – would oppose any moves that could stem the flow of foreign investment into the EU.[160] Yet, the specific issue of Chinese OFDI is particularly acute for these countries. Indeed, Finland, Sweden, and the Netherlands all rank in the EU top ten for amount of Chinese FDI received as a share of national GDP.[161] Not only are the free traders ideologically wed to the idea of economic openness, but they have disproportionately benefitted from Chinese FDI and have an interest in seeing investment flows continue.

Thus, it is unsurprising that the Nordics and the Netherlands have pushed back on Germany, France, and the Commission's calls for a stringent foreign investment screening mechanism. At a plenary session of the European Parliament in January, 2019, Finnish PM Juha Sipila criticized rising protectionism from some of the EU's "major players" – a not so subtle jab at Germany and France.[162] Even more substantially, the free traders formed an ad hoc coalition with a number of CEE and Mediterranean member states to water down the EU's original vision for a foreign investment screening mechanism.[163] As previously discussed, the foreign investment screening mechanism was first proposed by former EU Commission President Juncker in 2017 and aimed to emulate CFIUS by granting the Commission the power to review and potentially block problematic foreign investments into the EU. Despite being backed by Germany and France, two countries accustomed to getting their way in Brussels when they agree, the coalition of smaller member states successfully lobbied for a more toothless review mechanism. As a result, rather than bestowing the Commission with the power to block foreign

[160] "Foreign Direct Investment Regulatory Restrictiveness Index."
[161] See Chapter I for full top ten list
[162] Alexandra Brzozowski, "Implementation Key for Regaining Trust, Finland's PM Tells EU Lawmakers," *Www.Euractiv.Com* (blog), January 31, 2019, https://www.euractiv.com/section/future-eu/news/implementation-key-for-regaining-trust-finlands-pm-tells-eu-lawmakers/.
[163] Cerulus and Hanke, "Enter the Dragon."

investments unilaterally, the competence to vet foreign investment remains at the national level according to the final regulation. Though the regulation has been heralded as a success by the EU, the regulation falls well short of what was initially envisioned by leaving each national government in charge of FDI policy, even when investment is deemed risky and affects multiple member states.

Though not all members of the coalition cited Chinese investment as a reason to oppose a supranational screening mechanism, it clearly influenced the positions of a number of member states. Notably, a member of the Swedish Parliament's business and trade committee believed that Sweden's opposition to Juncker's proposal "could be linked to the fact that Sweden's two big carmakers [NEVS and Volvo] are owned by Chinese investors."[164] Similarly, during Council discussions of the proposal, Greek officials explicitly referenced Chinese investment as a reason for favoring a more lenient mechanism. The Greeks even went as far as to ask for compensation for the loss of investment from China that they would incur should a "protectionist" screening mechanism be adopted by the bloc.[165]

China's influence on the foreign investment screening discussions has been undeniable. A number of member states who have benefited from the influx of Chinese investment opposed a foreign investment screening mechanism that had the potential to stem the flow of Chinese investment into their countries. From the perspective of the member states who have welcomed Chinese OFDI, the regulation that was adopted in early 2019 represents a major victory. However, from the perspective of the EU as a single political and economic actor, the

[164] Ibid.
[165] Ibid.

current foreign investment review mechanism is not ideal. By leaving the competence to ultimately accept or block foreign investments to national authorities, the EU will continue to struggle to present a firm and unified position on FDI screening to China.

On a pragmatic level, the current FDI review mechanism may do little to stop investment deemed problematic, whether of Chinese provenance or not, from entering the EU. Though the new mechanism exhorts all member states to begin converging their national FDI screening regimes, it seems unlikely that all member states will adopt rigorous standards of review, let alone apply them strictly. Prior to 2017, only a handful of EU member states had any FDI review process in place, and they were seldom used to block inward investment.[166] In fact, by 2014, not a single Chinese investment into the EU had been blocked on the grounds of national security.[167] Since 2017, a number of member states have begun discussing the adoption of a dedicated FDI screening mechanism where one previously did not exist, but 11 member states – including Greece, Cyprus, and Malta – have made no movements to implement foreign investment screening mechanisms at all.[168]

Even in member states where foreign investments are screened, very few have blocked or threatened to block investments from China. As previously discussed, Germany has led the way in vigorously screening Chinese investment, blocking Chinese acquisitions of Aixtron in 2015 and of Leifeld Metal Spinning AG and 50Hertz in 2018. Though the French are yet to block any Chinese investments, in January, 2020, President Macron threatened to stop Jingye's

[166] Nicolas, "China's Direct Investment in the European Union."
[167] Zhang and Van Den Bulcke, "China's Direct Investment in the European Union."
[168] Hanemann, Huotari, and Kratz, "Chinese FDI in Europe: 2018 Trends and Impact of New Screening Policies."

proposed takeover of British Steel and investment in their Scunthorpe steelworks factory.[169] As was the case in Germany, the proposed blockage would come on the grounds of national security because British Steel's French operation supplies a large portion of track for the country's railway network. But to date, Germany and France's aggressive approach to screening FDI from China has been the exception, not the rule in the EU.

With the new FDI screening mechanism taking full effect in October 2020, there is still time for member states to alter their approach to screening foreign investment, especially foreign investment from China. But if the watering-down of the originally proposed screening mechanism and the subsequent lack of enthusiasm for implementing national screening mechanisms in many member states are anything to go by, it seems unlikely that FDI review standards will be harmonized and uniformly applied throughout the EU in the near future. As a consequence, the EU will not only be unable to prevent certain member states from accepting Chinese investment in strategic sectors, but they will be unable to fully leverage their power as a 27-country bloc to address the various challenges posed by Chinese OFDI.

Fractured EU Response to BRI

Chinese OFDI has created fissures in the EU in regards to BRI policy as well. While Brussels has generally been wary of BRI's arrival in Europe and in EU member states, not all member states have shared in Brussels' skepticism. The EU's concerns with BRI are

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[169] Rob Davies, "France Threatens to Block Chinese Firm's Rescue of British Steel," *The Guardian*, January 31, 2020, sec. Business, https://www.theguardian.com/business/2020/jan/31/france-threatens-to-block-chinese-firm-rescue-of-british-steel-jingye.

multifaceted, and many stem from the fact that seven years after being launched, BRI still lacks clarity in regards to its geographical scope and its classification for projects to be included in the initiative.[170] The EU has attempted to better understand BRI and its possible merits and drawbacks by commissioning a number of studies. One such study, conducted for the European Parliament's Tourism and Transport Committee, highlighted a number of areas of apprehension, including the sustainability of Chinese lending in certain countries, regulatory differences between the EU and China, and Chinese control of critical infrastructure.

One of the most commonly advanced concerns with BRI is the concept of "debt-trap diplomacy." Some western leaders, scholars, and commentators fear that Chinese lending practices may lead to debt distress in borrower countries, which China could then leverage for its own geopolitical gain. These fears are often buoyed by highly scrutinized BRI initiatives in Southeast Asia, such as China's takeover of the Hambantota Port in Sri Lanka after the Sri Lankan government was unable to repay its debts to the China Harbor Engineering Company.[171] A recent study from the Center for Global Development found that in most cases, BRI lending from Chinese financial institutions is unlikely to create systemic debt problems.[172] However, the same report identified Montenegro – a country currently in the EU accession process – as being at risk of defaulting on debt incurred as part of a BRI project linking the port city of Bar with

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[170] Astrid Skala-Kuhmann, "European Responses to BRI - An Overdue Assessment," *Horizons,* no. 14 (July 2019), http://www.cirsd.org/en/horizons/horizons-summer-2019-issue-no-14/european-responses-to-bri-an-overdue-assessment.
[171] Maria Abi-Habib, "How China Got Sri Lanka to Cough Up a Port," *The New York Times*, June 25, 2018, https://www.nytimes.com/2018/06/25/world/asia/china-sri-lanka-port.html.
[172] John Hurley, Scott Morris, and Gailyn Portelance, "Examining the Debt Implications of the Belt and Road Initiative from a Policy Perspective," CGD Policy Paper (Washington, DC: Center for Global Development, 2018), https://www.cgdev.org/sites/default/files/examining-debt-implications-belt-and-road-initiative-policy-perspective.pdf.

Serbia.[173] Given the EU's strict rules prohibiting sovereign debt from exceeding 60% of GDP and the memories of excessive borrowing feeding into the sovereign debt crisis, Chinese lending to Montenegro and to other EU member states is being watched carefully.[174]

Possibly of even greater concern to the EU are the differences between EU regulatory standards and Chinese regulatory standards. The EU prides itself on upholding rigorous environmental and labor standards when it comes to large construction projects. Thus, it is unsurprising that the EU fears these standards may be undermined by the different, and often lower, Chinese standards in large infrastructure projects, especially those taking place in third countries along the EU's periphery. To address these concerns, the study conducted for the Tourism and Transport Committee stresses that any cooperation between the EU's Trans-European Transport Network (TEN-T) and BRI must take place within a framework of "fair and undistorted competition based on regulatory convergence."[175] As noted in the previous chapter, the EU has also tried to address the dissonance in regulatory standards by promoting its own EU-Asia connectivity plan[176] as an "alternative" to BRI, as well as by introducing a handful of new initiatives that specifically aim to promote economic development in the Balkans.[177]

Finally, as has been noted previously, BRI investment has been heavily scrutinized due to its potential security implications. Chinese investment in critical infrastructure has been

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[173] Ibid.
[174] Liu, "Europe's Protectionist Position on the Belt and Road Initiative and Its Influence."
[175] Steer Davies Gleave, "Research for TRAN Committee: The New Silk Route - Opportunities and Challenges for EU Transport" (Brussels: European Parliament, Policy Department for Structural and Cohesion Policies, 2018), https://www.europarl.europa.eu/RegData/etudes/STUD/2018/585907/IPOL_STU(2018)585907_EN.pdf.
[176] European Commission, "Connecting Europe and Asia - Building Blocks for an EU Strategy."
[177] See, for example, the EU's "Berlin Process" or the "Enlargement Perspective for an Enhanced Engagement with the Western Balkans"

particularly prevalent in the Mediterranean, as China looks to make a number of European ports the western terminus of the Maritime Silk Road. COSCO's purchase of the Port of Piraeus, as well as their recent purchase of a 40% stake in Italy's Vado Port and agreement with the Port of Trieste have raised eyebrows in Brussels.[178] Investments in energy, from coal plants in Romania, to nuclear energy plants in the UK, and state grids in Portugal and Malta are equally as concerning to EU officials.[179]

Despite Brussels' persistent doubts surrounding BRI, response to BRI has lacked coherence throughout the EU. Institutionally, the EU has grappled with what the best level of participation with BRI is. EU leaders have attended diplomatic BRI summits and EU investment institutions such as the European Bank for Reconstruction and Development (EBRD) and European Investment Bank (EIB) have already partnered with China on a number of BRI projects.[180] Yet, the EU has also promoted its own transport network policy, TEN-T, and proposed alternatives to Chinese funding that align more closely with its own institutional values. The EU's difficulty in committing to a unified BRI policy is in part due to the ongoing difficulties in deciphering what exactly BRI is; it is challenging to address an initiative that is so sweeping yet remains poorly defined in practice. However, it has also been difficult for EU institutions to formulate a consistent BRI policy response because of divergent national views regarding BRI investment. Once again, there is a clear split between many of the EU's Northern

[178] François Godement et al., "China and the Mediterranean: Open for Business?" (European Council on Foreign Relations, June 21, 2017), https://www.ecfr.eu/publications/summary/china_and_the_mediterranean_open_for_business.
[179] Tartar, Rojanasakul, and Jeremy Scott Diamond, "How China Is Buying Its Way Into Europe."
[180] Skala-Kuhmann, "European Responses to BRI - An Overdue Assessment."

and Western member states who tend to endorse the Commission's skeptical stance and many Mediterranean and CEE countries who embrace BRI wholeheartedly.

At an official level, the EU has decided against signing a Memorandum of Understanding (MoU) with China regarding BRI, which would effectively institutionalize EU-China cooperation on BRI investments across the bloc. This has not stopped 18 of the EU's 27 member states from signing their own bilateral MoUs and actively courting infrastructure investment from Beijing. Predictably, BRI's incursion into Europe began on its eastern frontier. Poland was the first EU member state to sign a MoU in 2015, with many other CEE countries and non-EU member states such as Belarus, Ukraine, Serbia, Albania, and North Macedonia following suit.[181] As BRI has gained more momentum, its presence has been felt in Western Europe too. Indeed, the most recent spate of EU members signing on to BRI have included Portugal in late 2018, and Italy and Austria in early 2019. While the specific projects included in the framework of BRI cooperation vary slightly from country to country, the underlying motivations are the same: to encourage greater levels of Chinese investment and increase the volume of bilateral trade.[182] Generally speaking, the countries that have been receptive to BRI are those who are most desperate for investment, especially infrastructure investment, and those countries who have not enjoyed the same level of diplomatic engagement with China that the EU's larger member states have.

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[181] Liu, "The '16+1 Cooperation' under the 'Belt and Road' Initiative."

[182] Alicia Garcia Herrero and Jianwei Xu, "China's Belt and Road Initiative: Can Europe Expect Trade Gains?," Working Paper (Brussels: Breugel, 2016), https://www.bruegel.org/wp-content/uploads/2016/09/WP-05-2016.pdf.

On the other hand, nine member states have held out against pressure from Beijing to sign MoUs. This is not to say that all nine member states have scorned the opportunity to increase cooperation with China on infrastructure and trade-related issues. For instance, despite not formalizing their involvement with BRI via a MoU, Belgium has opened up new freight train lines with China, began collaboration with COSCO at the ports of Antwerp and Zeebrugge, and even agreed a deal with Alibaba to make Liege the conglomerate's first European logistics hub.[183] Other member states, such as Sweden, Finland, Denmark, Spain, Ireland and the Netherlands have maintained a "wait-and-see" policy, neither rejecting the premise of BRI outright nor actively looking to participate in an official capacity.[184] Finally, there are Germany and France, who once again have been the most outspoken opponents of BRI.

Germany and France's tougher stance on BRI mirrors their tougher stance on screening Chinese OFDI. These countries are not as hungry for Chinese investment and continue to highlight BRI's imperfections – a project procurement policy that continues to favor Chinese firms, fears over debt sustainability, and a general lack of transparency. As such, President Macron has vowed to approach BRI one investment at a time, and has pushed China to make sure all BRI investment in the EU is win-win.[185] German rhetoric toward BRI has been at times even less diplomatic, especially in the wake of Italy's embrace of the project. In response to the first G8 country joining BRI, German Foreign Minister Heiko Maas asserted that, "countries that

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[183] "China-Belgium Cooperation under BRI Makes Steady Progress," Belt & Road News (blog), April 10, 2019, https://www.beltandroad.news/2019/04/10/china-belgium-cooperation-under-bri-makes-steady-progress/.
[184] Mikael Weissmann, "Sweden's Approach to China's Belt and Road Initiative: Still a Glass Half-Empty," UI Brief (Swedish Institute of International Affairs, 2017), https://www.academia.edu/34691340/Sweden_s_approach_to_China_s_Belt_and_Road_Initiative_Still_a_glass_half-empty.
[185] Marine Pennetier and John Irish, "France Seals Multi-Billion Dollar Deals with China, but Questions Belt and Road Project," Reuters, March 25, 2019, https://www.reuters.com/article/us-france-china-idUSKCN1R61NF.

believe they can do clever business with the Chinese will wonder when they suddenly wake up in dependency."[186] Maas' comments may be extreme, however they reflect larger geopolitical concerns that BRI investment is not solely investment, but also a vehicle for China to increase its influence across the world and impose its own value system.[187]

Economic cleavages have always existed in the EU, whether it be between big and small member states, net contributors and net recipients, or debtors and creditors during the Eurozone crisis. In recent years, these cleavages have taken on a new dimension as Chinese OFDI has soared into the EU. Chinese investment has been seen by many member states – especially those who are less economically developed – as an important new source of capital. Yet member states do not evaluate the potential risks of Chinese OFDI identically. Germany and France have been leery of what the long-term drawbacks of Chinese investment may be for their respective countries and for the EU as a bloc, and thus have called for more caution vis-à-vis Chinese OFDI. However, other member states do not find these potential risks as credible, or if they do, have prioritized short-term needs for an investment boost over these concerns. This fault line, consequentially, has challenged the EU's internal cohesion and undermined the bloc's ability to approach key China policy issues with a unified voice.

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[186] "Chinese Investments in Europe: German EU Commissioner Floats EU Veto Right," Deutsche Welle, March 24, 2019, https://www.dw.com/en/chinese-investments-in-europe-german-eu-commissioner-floats-eu-veto-right/a-48045932.
[187] Meunier, "A Faustian Bargain or Just a Good Bargain?"

Chapter V – From Economic to Political Influence

Chinese OFDI has clearly deepened economic cleavages in the EU, making it difficult for the bloc to formulate a cohesive set of policies addressing the challenges posed by inward Chinese investment. But Beijing has also leveraged economic influence into increased political influence in the EU as well. The political implications of Chinese OFDI go beyond the issues directly pertinent to EU-China economic relations, such as the previously discussed investment screening mechanism and policy toward BRI. Indeed, Beijing has translated its economic relationship into political alliances with many of the EU's more illiberal, Eurosceptic leaders, who now find they have an ally outside of Brussels. Even more striking, China has used its economic power to gain important political concessions on issues such as receiving the Dalai Lama, the South China Sea conflict, the Hong Kong protests, and various human rights concerns.

An Ally to Eurosceptical and Illiberal Leaders

In the EU, some of China's most amicable bilateral relations are with member states that are increasingly illiberal, Eurosceptical or some combination thereof. This is not to say that China is intentionally trying to promote illiberalism and Euroscepticism across the bloc as a way to undermine the EU. In fact, what seems more likely is that member states that feel increasingly ostracized or neglected by Brussels – which are often the same member states hungry for foreign investment – have been drawn to China. But in either case, it is clear that

China has been more than happy to embrace its role as an alternative to the liberal, cooperative, Brussels-based order.[188]

China as a political and economic alternative to the EU has been especially attractive for some of the EU's increasingly illiberal member states. Hungarian Prime Minister Viktor Orbán and Poland's Law and Justice party have come under fire for subverting the rule of law and a litany of other "breaches" of core EU values.[189] As a result, the EU has repeatedly threatened to impose economic sanctions on both countries if they fail to address democratic backsliding. It is unsurprising then, that both countries have worked hard in recent years to nurture their economic and political relationships with Beijing; China's political and economic cooperation, in contrast to the EU's, does not contain the political conditionalities of good governance and liberal economic reform.[190] In both Hungary and Poland, leaders have cozied up to China by hosting a number of high-level Chinese officials and signing increasingly involved cooperation agreements.[191] Prime Minister Orbán has gone even further, most notably at a 2016 China-CEE Political Parties Dialogue when he delivered a speech criticizing EU integration and endorsing China's rejection of universal values and norms.[192]

A number of other EU leaders skeptical of the European project have bolstered their relationships with China in recent years too. A glaring example is Czech President Milos Zeman,

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[188] Benner et al., "Authoritarian Advance."
[189] Leonid Bershidsky, "How the EU Plans to Punish Hungary and Poland," Bloomberg.com, January 18, 2019, https://www.bloomberg.com/opinion/articles/2019-01-18/how-the-eu-plans-to-punish-hungary-and-poland.
[190] Benner et al., "Authoritarian Advance."
[191] Marcin Goettig, "Xi Welcomes Chinese Freight Train to 'strategic Partner' Poland," Reuters, June 20, 2016, https://www.reuters.com/article/uk-poland-china-xi-idUKKCN0Z6205.
[192] Hungarian Government, "Viktor Orbán's Speech at the Conference 'China-CEE Political Parties Dialogue,'" October 6, 2016, https://www.kormany.hu/en/the-prime-minister/the-prime-minister-s-speeches/viktor-orban-s-speech-at-the-conference-china-cee-political-parties-dialogue.

who since coming to power in 2014 has aggressively pursued improved relations with China. He has gone beyond the reverent rhetoric and historic bilateral summits with China typical of many EU leaders. Indeed, he was the only Western leader to attend a 2016 military parade in Beijing celebrating the anniversary of the end of World War II.[193] Furthermore, he appeared on Chinese television, stating that Czech submissiveness to the EU had been preventing a Czech-Chinese rapprochement.[194]

As Zeman's comment would suggest, his kowtowing to Beijing has been accompanied by a domestic platform of Euroscepticism. He has consistently denigrated the EU's treatment of the Czech Republic and in 2016 even proposed a referendum to exit the EU. The likes of Poland, Hungary, and the Czech Republic might represent the most extreme cases of member states disparaging the EU while simultaneously nurturing their relationship with Beijing, but subtler examples of this trend are visible in other member states as well. Eurosceptic leaders such as Italian Prime Minister Matteo Salvini and former Greek Prime Minister Alexis Tsipras have prioritized their relationship with China, and leaders of German right-wing parties such as Alternative für Deutschland (AfD) and Bürgerrechtsbewegung Solidarität (BüSo) have adopted official Chinese political language as part of their campaigns to criticize Chancellor Merkel.[195]

China's improved relationships with a number of vexing EU leaders is concerning for the EU for a few reasons. On a pragmatic level, the EU could lose some of its economic leverage over countries under censure because they have a newfound, wealthy ally whose capital does

[193] Robert Muller and Jan Lopatka, "Czech Courtship Pays off with Landmark Visit from Chinese Leader," Reuters, March 28, 2016, https://www.reuters.com/article/us-czech-china-idUSKCN0WU01J.
[194] Kalyeena Makortoff, "China Visit Marks Czech 'Vulnerability': Analyst," CNBC, March 29, 2016, https://www.cnbc.com/2016/03/29/china-visit-marks-czech-vulnerability-analyst.html.
[195] Benner et al., "Authoritarian Advance."

not have good-governance strings attached. Just as Viktor Orbán has explicitly stated, EU member states may now be able to turn to China as an alternative for funding if they feel Brussels is being unaccommodating. But perhaps even more importantly, China's close economic and political partnership with leaders skeptical of the European project is harmful to EU political unity. On a symbolic level, China's approval of illiberal and Eurosceptic leaders, whether overt or tacit, legitimizes their views and empowers them to hold firm against Brussels. These Eurosceptic leaders may no longer feel alienated and powerless against Brussels knowing they have the support of China. In essence, not only does the Chinese economic and political model provide ideological fodder for leaders questioning the validity of the EU's normative prescriptions, but it represents a convenient piece of leverage during negotiations with Brussels and other EU-friendly governments.[196] Once again, it should be remembered that the basis for China's improved relations with many EU governments has been the promises of increased investment levels. It is from these original economic arrangements that deeper diplomatic and political ties emerge.

Chinese political influence manifests itself not only in the emboldening of Eurosceptic and illiberal governments, but also in more visible and substantive ways. Indeed, China has parlayed its economic presence throughout the bloc into support from many EU member states on political issues important to China. This support goes beyond economic issues directly addressing China, such as the FDI screening mechanism that was watered down by a coalition of member states, to include key geopolitical and human rights concerns. This pattern of economic might influencing political decision-making has been well-documented outside of

[196] Ibid.

Europe – most notably in Latin America and Africa[197] – but it now appears that China has effectively been able to wield OFDI as a carrot and a stick within the EU as well.

The Dalai Lama Question

Perhaps the most prominent example of China shaping EU member state policy on a salient political issue is in regards to the Dalai Lama. A 2013 paper by Fuchs and Klann found that countries whose leadership received the Dalai Lama saw exports to China subsequently dip as a punishment.[198] European countries have been no exception to this economic punishment from China. In fact, as countries have come to value courting Chinese OFDI, in addition to boosting bilateral trade, deference to China on the Dalai Lama issue has been all the more visible. In 2012, China cancelled a number of ministerial meetings with the UK, including with the UK Trade and Investment Minister, due to David Cameron's meeting with the Dalai Lama just a month prior.[199] More recently, Slovakia's ambassador to Beijing sent a letter to Chinese Foreign Minister Wang Yi, apologizing for their country's reception of the Dalai Lama in 2016 and reaffirming their respect for China's territorial integrity.[200] The letter was only sent after Chinese Premier Li Keqiang cancelled a bilateral meeting with Slovakian Prime Minister Robert Fico and the economic and diplomatic price of the Dalai Lama's visit became clear.

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[197] Meunier, "A Faustian Bargain or Just a Good Bargain?"
[198] Andreas Fuchs and Nils-Hendrik Klann, "Paying a Visit: The Dalai Lama Effect on International Trade," *Journal of International Economics* 91 (2013): 164–77, http://dx.doi.org/10.1016/j.jinteco.2013.04.007.
[199] Meunier, "A Faustian Bargain or Just a Good Bargain?"
[200] Benner et al., "Authoritarian Advance."

The most striking example of an EU government changing policy on the Dalai Lama to accommodate China's foreign policy wishes is the Czech Republic. Thanks in part to Vaclav Havel's legacy, the Czech Republic has for a long time been one of the EU's most outspoken defenders of human rights and has historically welcomed the Dalai Lama to Prague with open arms.[201] But in 2016, President Zeman, along with Prime Minister Sobotka and the heads of the Czech parliament's upper and lower chambers issued a public statement reprimanding three high-level minsters who had met with the Dalai Lama. The uncle of one of the censured ministers, a Holocaust survivor, was even withheld a government medal by President Zeman because of his nephew's actions.[202] Curiously, the joint statement rebuking the three ministers was preceded by a confidential visit to Prague Castle – the seat of the Czech President – by Chinese Ambassador Ma Keqing."[203] Though the Czech government did not officially acknowledge the reason for abruptly changing policy on receiving the Dalai Lama, it is clear that a combination of Chinese pressure and proactive efforts to endear themselves to Beijing were central considerations.

A Lack of Consensus

China's economic sway over the bloc could also be seen in a 2016 ruling regarding territorial disputes in the South China Sea. After an international panel in The Hague ruled in favor of the Philippines and against China, EU members quibbled for 72 hours over the contents

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[201] "Gaining Wisdom, Marching Forward."
[202] Barboza, Santora, and Stevenson, "China Seeks Influence in Europe, One Business Deal at a Time."
[203] Benner et al., "Authoritarian Advance."

of a joint statement addressing the ruling.[204] EU foreign policy chief Federica Mogherini's final statement was a lowest common denominator statement, one that did not explicitly mention China, let alone take a critical stance toward them. Instead, Mogherini's statement read: "While not taking a position on claims to land territory and maritime space in the South China Sea, the EU urges all claimants to resolve disputes through peaceful means, to clarify the basis of their claims, and to pursue them in accordance with international law including UNCLOS and its arbitration procedures."[205] Mogherini's statement marked a significant departure from the EU norm of supporting international law and the United Nations in the majority of its foreign policy stances. One EU diplomat even called the statement "shameful" due to its lack of criticism of China.[206]

But Mogherini's toothless statement on behalf of the EU was more a reflection of the stance of a few EU member states rather than the whole bloc. Releasing a foreign policy statement requires consensus among EU members, and three members – Hungary, Greece, and Croatia – required the EU to revise down its original statement.[207] Croatia favored a watered-down statement due to its own ongoing territorial disputes with Slovenia over the Gulf of Piran,[208] but Hungary and Greece's refusal to support a statement critical of China evince Beijing's influence over the two member states. Indeed, diplomats involved in the discussion

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[204] Laurence Norman, "EU Issues South China Sea Statement Ending Discord Within Bloc," *Wall Street Journal*, July 17, 2016, https://www.wsj.com/articles/eu-issues-south-china-sea-statement-after-failing-to-agree-common-stance-1468583961.
[205] Federica Mogherini, "Declaration by the High Representative on Behalf of the EU on Recent Developments in the South China Sea," European Council, March 11, 2016, http://www.consilium.europa.eu/en/press/press-releases/2016/03/11/hr-declaration-on-bealf-of-eu-recent-developments-south-china-sea/.
[206] "Gaining Wisdom, Marching Forward."
[207] Le Corre, On China's Expanding Influence in Europe and Eurasia.
[208] Croatia anticipated a ruling in Slovenia's favor and thus felt disinclined to recognize rulings from international tribunals on maritime border disputes. The tribunal did rule in Slovenia's favor in 2017.

regarding the joint statement noted that concerns about harming economic ties with China factored into the debate.[209] Additionally, before The Hague's decision, former Greek Prime Minister Alexis Tsipras was invited to Beijing for five days to discuss, among a variety of topics, the upcoming ruling.[210] One day after Mogherini's statement, Hungary broke ranks again by issuing its own individual statement on the ruling that clearly sided with China. The statement asserted that "countries should settle disputes 'through direct negotiations' and that 'external pressure and interference may have an adverse effect on the current situation.'"[211] Clearly it is no coincidence that two of the member states most fearful of upsetting China and possibly losing investment were those that defected from the common EU position.

Lack of EU consensus on China-related issues is not an isolated event. Rather, the EU has been unable to release statements regarding various Chinese human rights abuses in recent years due to individual member states dissenting. And once again, the main culprits have been Greece and Hungary. In 2017, Greece was the only EU member state to veto a statement condemning China's human right's record at the UN Human Rights Council (UNHCR). Greek officials claimed the statement was an "unconstructive criticism of China,"[212] and that EU-China dialogues on human rights would be a "more efficient and constructive way of delivering better results."[213] In a similar situation, Hungary prevented the EU from releasing a joint letter in 2017

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[209] Norman, "EU Issues South China Sea Statement Ending Discord Within Bloc."
[210] Ibid.
[211] Theresa Fallon, "The EU, the South China Sea, and China's Successful Wedge Strategy," Asia Maritime Transparency Initiative, October 13, 2016, https://amti.csis.org/eu-south-china-sea-chinas-successful-wedge-strategy/.
[212] "Gaining Wisdom, Marching Forward."
[213] *Quoted in* Helena Smith, "Greece Blocks EU's Criticism at UN of China's Human Rights Record," *The Guardian*, June 18, 2017, https://www.theguardian.com/world/2017/jun/18/greece-eu-criticism-un-china-human-rights-record.

condemning China's practice of detaining and torturing human rights lawyers.[214] According to EU diplomats, Hungarian officials even threatened to block all future joint declarations criticizing Beijing's human rights record.[215] The EU's inability to release joint statements challenging China's human rights abuses is particularly worrying given the implications for the bloc's reputation. The EU has for many years prided itself on being a staunch defender of liberal values such as peace, inclusivity, and human rights. The EU was even awarded the Nobel Peace Prize in 2012 for its six-decade commitment to the "advancement of peace and reconciliation, democracy, and human rights in Europe."[216] As is such, Greece and Hungary's blockage of joint declarations has been deeply frustrating to many EU officials.

Despite the outcry over Greece and Hungary's defection from the EU's critical position toward China on a number of issues, recent developments in Hong Kong and Xinjiang indicate that the bloc is no closer to presenting a unified voice on human rights issues than in previous years. As protests in Hong Kong over political independence from Beijing have boiled over, pro-China riot police have been accused of a number of human rights abuses, including firing upon and killing protestors. In response, whereas the US Congress passed a 2019 bill imposing sanctions on those responsible for human rights violations in Hong Kong, the EU's response has been relatively muffled. In July 2019, the European Parliament passed a non-binding resolution

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[214] Le Corre, On China's Expanding Influence in Europe and Eurasia.
[215] Simon Denyer and Emily Rauhala, "Eleven Countries Signed a Letter Slamming China for Torturing Lawyers. The U.S. Did Not.," *Washington Post*, March 22, 2017, https://www.washingtonpost.com/news/worldviews/wp/2017/03/22/eleven-countries-signed-a-letter-slamming-china-for-torturing-lawyers-the-u-s-did-not/.
[216] Ingi Iusmen, *Children's Rights, Eastern Enlargement and the EU Human Rights Regime* (Manchester: Manchester University Press, 2014), https://www.jstor.org/stable/j.ctt18mbg21.12.

that called for an investigation into police violence in Hong Kong, and in November 2019 the Commission called for de-escalation following the siege of Hong Kong Polytechnic University.[217]

The EU's mild response to the events unfolding in Hong Kong has once again been influenced by economic relations with China. In this case, there has not been one distinct group of countries vocally opposed to a tougher line on China. Instead, Brussels has seemed reluctant to do anything more than issue statements that implore China to de-escalate and that reaffirm political support for Hong Kong. A number of anonymously quoted EU diplomats confirmed that recalcitrance across the bloc stemmed from fear of retaliation from China – which they witnessed in response to the US Congress's "Hong Kong Human Rights and Democracy Act."[218] One diplomat was even quoted as saying "there is little more that can be done. At the end of the day, I fear that the economic relationship with China is just too important."[219] The fact that this sentiment appears to be widespread in the case of the Hong Kong protests, rather than confined to a few EU member states, is worrying for the bloc. Even France, who are one of the most outspoken voices on China, attempted to tamp down on official criticism of the Hong Kong police before President Macron's four-day visit to China.[220] In essence, China's economic leverage has successfully prevented one of the world's foremost human rights advocates from taking significant action in response to clear human rights violations.

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[217] Keegan Elmer, "Europe 'Reluctant to Act over Hong Kong for Fear of Beijing's Response,'" *South China Morning Post*, November 20, 2019, https://www.scmp.com/news/china/diplomacy/article/3038633/europe-reluctant-do-more-about-hong-kong-fear-beijings.
[218] "China Slams 'criminal' EU Response to Hong Kong Clampdown," *Al Jazeera*, October 7, 2019, https://www.aljazeera.com/news/2019/10/china-slams-criminal-eu-response-hong-kong-clampdown-191007110105021.html.
[219] *Quoted in* Elmer, "Europe 'Reluctant to Act over Hong Kong for Fear of Beijing's Response.'"
[220] "China Slams 'criminal' EU Response to Hong Kong Clampdown."

The story has been similar regarding the EU's response to the detention of Uighurs and other ethnic minorities in China's Xinjiang province. A number of UN reports have denounced the "re-education camps" that have proliferated in Xinjiang and called upon China to allow independent monitors to access the province.[221] Up until December 2019, the EU's response toward the treatment of the Uighur people has been restrained. Foreign policy chief Federica Mogherini reiterated the UN's call for both independent monitors and an investigation while urging member states to open their borders to Uighur asylum-seekers. So far, only Sweden has heeded her calls by granting all Uighur asylum-seekers refugee status, and individual member states have either voiced muted concerns regarding the situation in Xinjiang or said nothing at all.[222]

In July 2019, 15 of the EU's 27 member states signed a letter to the UN High Commissioner for human rights condemning China's actions in Xinjiang, but a lack of bloc-wide solidarity on the issue prevented a joint letter from the whole EU being released.[223] In fact, the 12 countries that did not sign the letter – Italy, Bulgaria, Croatia, Cyprus, Malta, Portugal, Romania, Slovakia, Slovenia, Greece, Hungary, and the Czech Republic – are all Southern or CEE member states that have thirsted for Chinese investment and often split with Brussels on key China-related issues. A European Parliament resolution passed in December 2019 was the most

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[221] David Marques, "The EU, China, and Human Rights in Xinjiang: Time for a New Approach," Commentary (European Council on Foreign Relations, April 2, 2019), https://www.ecfr.eu/article/commentary_the_eu_china_and_human_rights_in_xinjiang_time_for_a_new_approach.

[222] Ibid.

[223] Saulius Jakucionis, "Europe Split on China – Lithuania Joins 15 EU States Condemning Beijing's Treatment of Uighurs," Lithuanian Radio and Television, July 22, 2019, https://www.lrt.lt/en/news-in-english/19/1080713/europe-split-on-china-lithuania-joins-15-eu-states-condemning-beijing-s-treatment-of-uighurs.

unequivocal rebuke of Beijing's treatment of the Uighur and other ethnic minorities in Xinjiang. However, the resolution once again falls short of taking any concrete action.[224]

Interestingly, on the issue of Taiwan, EU member states do not seem to be particularly swayed by Chinese influence. The EU adheres to a long-standing "One China" policy, which means that the bloc has no diplomatic or formal political relations with Taiwan. The EU does however have structured dialogue with Taipei, supports their participation in international fora, and maintains a strong economic relationship with the island.[225] Plus, in recent years, a number of member states have looked to work within the One China framework to deepen their relations with Taiwan. Taiwanese officials have been hosted in a number of European capitals, and numerous governments have voiced a desire to include Taiwan in more international organizations. For example, in October 2019, the Dutch Parliament passed a motion supporting Taiwanese participation in international fora.[226] Sweden, who were urged not to air a documentary about democracy in Taiwan on Swedish television by the Chinese embassy, did not bow to the pressure and continue to call for greater Taiwanese participation in a number of international organizations.[227]

Even the Czech Republic, which has in many cases prioritized investment from China over other human rights and geopolitical considerations, have stood strong on the Taiwan question. In response to the city of Prague signing a cooperation agreement with Taiwan and

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[224] European Parliament, "Situation of the Uyghur in China," P9_TA(2019)0110 § (2019), https://www.europarl.europa.eu/doceo/document/TA-9-2019-0110_EN.html.
[225] European Commission, "Taiwan - Trade," 2019, https://ec.europa.eu/trade/policy/countries-and-regions/countries/taiwan/.
[226] Pei-ju Teng, "Dutch Parliament Passes Motion Supporting Taiwan's International Participation," *Taiwan News*, October 9, 2019, https://www.taiwannews.com.tw/en/news/3792841.
[227] Yi-hsuan Lu and William Hetherington, "China Slams Report on 'Taiwan Democracy,'" *Taipei Times*, March 12, 2019, http://www.taipeitimes.com/News/taiwan/archives/2019/03/12/2003711334.

the Czech Senate Speaker, Jaroslav Kubera, planning to visit Taiwan, Beijing responded with a salvo of economic threats. These included cancelling the Prague Philharmonic Orchestra's tour of China, revoking a promise to the Prague city zoo to host a panda, and directly threatening Czech companies operating in China.[228] In fact, a letter sent by China's embassy in Prague to the Czech president's office stated that "Czech companies who have economic interests in China will have to pay for the visit to Taiwan by Chairman Kubera."[229] Interestingly, President Zeman has shown reluctance to get involved in the Prague-China spat and so far has not publicly called upon Chairman Kubera to cancel his trip.

Given the complexity of China's economic statecraft, it is difficult to definitively say that access to Chinese investment has been the motivating force for defection on key consensus issues in the EU. Indeed, China seems to leverage its whole economic package – volume of bilateral trade, OFDI, access to the Chinese market, and more generally good economic and diplomatic relations – as a way to force compliance from other countries. But in the case of EU countries such as Hungary, Portugal, Greece, and the Czech Republic, Chinese investment seems to be the biggest carrot. Not only have these member states specifically voiced a need for foreign investment, but they have received a disproportionately large share of Chinese OFDI in the EU given the size of their respective economies. Moreover, whereas Chinese OFDI in these countries has taken off in the past decade, increases in bilateral trade, in most cases, have been more modest. According to the IMF's Direction of Trade Statistics, in both Hungary

[228] Peter Laca, "China's Ties With Key European Ally Nosedive Over Taiwan," Bloomberg.com, January 14, 2020, https://www.bloomberg.com/news/articles/2020-01-14/china-s-ties-with-key-european-ally-nosedive-over-taiwan.
[229] Raphael Satter and Nick Carey, "China Threatened to Harm Czech Companies over Taiwan Visit: Letter," Reuters, February 19, 2020, https://www.reuters.com/article/us-china-czech-taiwan-idUSKBN20D0G3.

and Greece, the volume of bilateral trade has remained almost identical since 2008, and the volume of bilateral trade between Portugal and China has increased by roughly $1 billion over the past decade. The Czech Republic is the exception, seeing both the volume of imports from China and exports to China more than double over the past decade. Once again, it is difficult to disentangle the OFDI effects and trade effects on the shift in political stance of certain EU leaders, however, the timing of these political defections coincides with a period in which Chinese investment in these member states has skyrocketed.

Brussels' reluctance to take meaningful measures against Beijing out of fear of damaging economic relations, as well as the defection of a few particularly China-friendly member states on consensus issues, is indicative of how China has turned economic relations into political leverage. This leverage has been particularly acute in some of the EU's smaller member states and those that may feel maligned by Brussels. The pattern of using economic power, and in particular promises of investment and increased trade, to gain concessions on human rights and geopolitical issues is not without precedent. A 2017 Human Rights Watch report detailed how China "seeks to exert economic and political pressure on countries to obtain its goals," with smaller and poorer countries as the main target.[230] Their efforts have often been effective, as aid-dependent African nations have refused to criticize Beijing's human rights record and countries such as Panama and Sao Tome and Principe announced in 2016 that they would sever diplomatic ties with Taiwan.[231] Even in the US, China has used its economic

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[230] "The Costs of International Advocacy | China's Interference in United Nations Human Rights Mechanisms" (New York: Human Rights Watch, September 5, 2017), https://www.hrw.org/report/2017/09/05/costs-international-advocacy/chinas-interference-united-nations-human-rights.
[231] Mike Ives, "A Small African Nation Severs Ties with Taiwan, and Beijing Applauds," *The New York Times*, December 22, 2016, https://www.nytimes.com/2016/12/22/world/asia/china-taiwan-sao-tome-principe.html;

power for political ends. Hollywood studios, major companies, and most recently, the National Basketball Association (NBA) have kowtowed to Beijing on politically salient issues in order to retain lucrative market access.

China has demonstrated its ability to parlay economic relations into political support across the world, but the trend is particularly worrying in the EU. In one respect, it is worrying because Beijing has positioned itself as an ally of EU member states that are either subverting EU values or questioning the continued validity of the European project. China does not invest nearly as much in frustrated EU countries as these countries receive in transfer payments from Brussels, but what China lacks in investment quantity they make up for in political nous; China does not attach any conditionalities of good governance to their OFDI which many illiberal and Eurosceptic leaders find chafing, and the bilateral nature of their relationships confers a sense of importance on smaller member states that they do not usually experience at the EU level. China's increasing political influence in the EU is also concerning because it threatens the EU's prospects for cohesion on key foreign policy issues. The allure of Chinese OFDI has stifled attempts to implement supranational FDI screening, a unified policy toward BRI, and even action on human rights violations, of which the EU has been a longstanding champion.

Cindy Sui, "Panama Cuts Ties with Taiwan for China," BBC News, June 13, 2017, https://www.bbc.com/news/world-latin-america-40256499.

Conclusion

The inrush of Chinese OFDI into the EU has been nothing short of remarkable. In the past decade, Chinese investment in EU member states has increased from $1 billion per annum to over 40 times that. Investment has been concentrated in the EU's most robust economies although some of the bloc's smaller member states have been the biggest beneficiaries of Chinese OFDI when measured as a share of host country GDP. Chinese OFDI in the EU has also been quite idiosyncratic, with total investment volume, SOE share of investment, and regional destination of investment within the EU varying noticeably year to year. Some of the idiosyncrasy in Chinese OFDI trends can be chalked up to what mega-deals were agreed upon in any given year; roughly 95% of Chinese OFDI in the EU has taken the form of M&As and a couple of large deals can dramatically reshape the yearly OFDI landscape in the EU. But the idiosyncrasy of Chinese investment in the EU is also a reflection of the unique nature of Chinese OFDI.

Chinese investment into the EU stands out for a variety of reasons. For one, Chinese OFDI into the EU is a rare case of a less-developed economy investing in a more-developed economy. As such, the dynamics of China's investment in the EU break from the paradigm of FDI decision-making. Though there is still disagreement in the literature, it appears that Beijing's strategy of supporting Chinese firms to acquire high-tech EU firms is predominately an asset-seeking strategy rather than a market-seeking one. Indeed, the pattern of large Chinese firms buying up European firms in critical industries is a way to gain both managerial and technological knowhow. Beijing has made a concerted effort, as evidenced by their succession of five-year plans, to make domestic firms more competitive in international markets and move production up the value chain. The EU is an ideal location for Beijing to focus its OFDI precisely because it possesses the assets required to upgrade Chinese industry – a raft of high-tech manufacturing firms, managerial prowess, and globally recognized brands.

As the EU faced economic stagnation in the wake of the GFC, Chinese OFDI was welcomed and even courted aggressively in certain member states. But as the short term need for a capital influx dwindled and the EU began to appreciate some of China's underlying motivations for investing in the bloc, Brussels reformulated its stance on Chinese investment practices. In particular, the rapid rise of Chinese OFDI across the EU highlighted the lack of reciprocal market access that EU firms have in China and exposed fears over the security implications of Chinese penetration in strategic EU sectors, such as high-tech manufacturing, dual use technologies, and critical infrastructure. To a certain extent, as Sophie Meunier states it, Chinese OFDI had a centripetal effect on the EU.[232] In response to Beijing's investment practices – which Brussels recognized may be benefitting Chinese firms at the EU's expense – the bloc is continuing to push China to sign a bilateral investment treaty and implemented an FDI screening mechanism.

Though Brussels has recognized the challenges of Chinese OFDI for the bloc and member states have come together to begin addressing them, Chinese investment has had significant centrifugal effects as well. Chinese OFDI has deepened pre-existing economic cleavages between member states and sowed new divisions across the bloc. It has become increasingly clear that not all member states analyze the costs and benefits of Chinese OFDI

[232] Meunier, "Divide and Conquer? China and the Cacophony of Foreign Investment Rules in the EU."

uniformly. Some of the bloc's larger and wealthier member states – Germany and France in particular – have been the most outspoken skeptics of Chinese OFDI whereas many of the smaller EU economies on the bloc's fringes have continued to woo Chinese capital.

Differences in member state opinion vis-à-vis Chinese OFDI has made collective action difficult. Though the EU did adopt an FDI screening mechanism, it was watered-down by a number of investment-hungry member states so as to essentially keep the competence over FDI screening at the national level. Similarly, disagreement over the potential value of BRI for the EU has inhibited the creation of a coherent EU policy toward the initiative. Chinese OFDI has also hampered the EU's ability to address foreign policy issues that go beyond China's investment practices. In fact, Beijing has leveraged its economic relationship with a number of the EU's smaller member states – many of whom have Eurosceptic leaders at the helm – to gain concessions on foreign policy concerns important to China.

Given China's ability to parlay OFDI into influence in both the EU and other regions of the world, commentators continue to grapple with the underlying motivations for Beijing's economic statecraft. The phrases "divide and conquer" and "divide and rule" have become nearly ubiquitous with China's strategy for dealing with the EU, especially among European thing-tankers such as Le Corre, Parello-Plesner, Godement, and Benner. While it is clear that Chinese OFDI has at times divided the bloc by exacerbating fault lines between member states – most notably between the wealthier member states less hungry for investment and more concerned with security and the poorer member states in which a desire for FDI trumps other considerations – it is not clear that Beijing intends to conquer or rule the EU. Even more importantly, it is not clear what exactly most commentators even mean by the terms "conquer" or “rule.” It seems unlikely that China’s overarching ambition is to dominate the EU in a grand strategy sense of the word or to throw the future of the European project into jeopardy. Rather, this author is of the opinion that China’s strategy for dealing with the EU boils down to self-interest and pragmatism; Beijing engages with EU member states in a way that helps it best achieve its own domestic and foreign policy goals.

Commentators who look cynically upon China’s economic statecraft in the EU often highlight China’s propensity to work bilaterally with EU member states or develop its own sub-regional fora, such as 16+1 format, instead of working directly with Brussels. It is undeniable that China has consistently prioritized bilateralism and shirked Brussels, but from the Chinese perspective this approach makes the most sense. On one hand China sees the EU as a slow-paced decision-making body comprised of disparate national interests, and thus it is more effective to deal with member states on an individual basis.[233] Plus, official China-EU summits have yielded increasingly unfavorable outcomes from a Chinese perspective; Brussels has become more critical in their rhetoric toward China in recent years and have pursued policies inimical to Chinese interests. On the other hand, China understands that it can use differences in member state priorities to achieve lowest common denominator outcomes that benefit China. As Parello-Plesner notes:

> “Even before the euro crisis, China knew how to employ the EU’s multi-level governance to its advantage based on differences between member states within the EU. For example, China knows that Southern European countries aren’t likely to be frontrunners on EU’s human rights policy, and that free-traders in the North,

[233] Shi Zhiqin, “Understanding China-EU Relations,” Carnegie Europe, October 15, 2012, https://carnegietsinghua.org/2012/10/15/understanding-china-eu-relations-pub-49688.

> spearheaded by the UK, Netherlands, Denmark, and Sweden will work to block strong retaliatory moves on trade that smack of protectionism."[234]

In essence, China recognizes the expediency of working with EU member states individually or in small groups rather than working directly with Brussels. Beijing is not blind to the fact that it may be sowing the seeds of greater disunity in the EU on a variety of political and economic issues. However, EU disunity on these issues is not an end unto itself per se, but rather a means to advance Beijing's own interests, such as a greater investment access to the EU market and less pushback from the EU on salient political issues.

Seen in this light, the challenge that Chinese OFDI poses for the EU is not a wholly new challenge. In fact, many of the EU's allies and foes recognize that the EU is much stronger when negotiating as a united bloc and thus attempt to circumvent Brussels. The Trump administration has consistently floated the idea of negotiating bilateral trade agreements with individual member states, namely Germany, as a way to secure "better deals" for the US.[235] An even more glaring example is Russia's Nord Stream 2 pipeline negotiations. Despite the new liquid natural gas pipeline being ardently opposed by a number of CEE member states as well as the former President of the European Council Donald Tusk, Russia has worked with supportive EU governments to push the project forward.[236] Working with the whole bloc on Nord Stream 2

[234] J Parello-Plesner, "China and Europe in the Eurocrisis," § US-China Economic and Security Review Commission (2012), https://www.uscc.gov/sites/default/files/transcripts/4.19.12HearingTranscript.pdf.
[235] Linette Lopez, "Trump Repeats Idea That Germany Can Negotiate Trade Outside of EU," Business Insider, March 18, 2017, https://www.businessinsider.com/trump-repeats-claim-that-germany-can-negotiate-trade-outside-of-eu-2017-3.
[236] Peter Teffer, "Tusk: Nord Stream II Doesn't Help," EUobserver, December 18, 2015, https://euobserver.com/energy/131605.

would be slow, and most likely unsuccessful, so Russia has chosen to work directly with a subset of willing member states.

In some ways the challenge posed by Chinese OFDI is unique, given that China is an ascendant power with a mixed economy adept at leveraging its economic strength for greater geopolitical gain. But in another sense, the EU's struggles to address China's investment practices and its growing influence across the bloc is a challenge rooted in the EU's institutional composition. The 27 member states that comprise the EU all face unique domestic macroeconomic conditions. Consequentially, each country has different economic priorities and weighs the pros and cons of Chinese OFDI differently. While Germany, a net exporter, may prioritize protecting its high-tech manufacturing industry and getting China to reciprocate market access, smaller countries recovering from economic crisis or struggling with persistent slow growth may see attracting foreign capital as their primary objective. Yet, despite these varied and often times competing economic interests, the biggest issues affecting the bloc require consensus. Thus, the influx of Chinese OFDI in the EU is a complex, multidimensional phenomenon. It is at once a savior for floundering EU countries and companies, a tool of Beijing's economic statecraft, a challenge for Brussels bureaucrats, and above all else, a reminder of the EU's institutional limitations.

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