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# Towards a Geopoliticization of Investment Policy? Investment Screening in the European Union

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## Abstract

Against the background of rapidly rising levels of Chinese foreign direct investment in the first half of the 2010s until 2016, the EU adopted an investment screening framework regulation in March 2019 to coordinate investment screening policies. The regulation defined criteria according to which its member states can block Chinese FDI due to security and public order concerns in several areas, including critical infrastructure. The paper analyses whether this policy change originated in a changing perception of longer-term European economic interests when facing increased high-tech competition and might reflect domestic demands for protectionism from private actors; or was it rather driven by growing security concerns of public actors reflecting a more geopolitical interpretation and framing of EU-China economic relations? Germany, a key destination of surging Chinese FDI in the EU between 2010 and 2016, had a pivotal role as an agenda setter and driver of this EU-level policy change. Hence, the paper puts a special emphasis on disentangling economic and security interests as explanatory factors accounting for preference formation and policy change in Berlin.

Keywords: European Union; Germany; China; Trade Policy; Investment Screening; Economic Security.

## Introduction[1]

> 'As regards China: We cannot disentangle economic and geopolitical questions'
> (Annalena Baerbock, German Foreign Minister)[2]

In recent years, we have seen an international trend towards more intensive control and screening of foreign direct investment (FDI) in many Western states (Lenihan 2018). In the EU, too, changes in legislation occurred both at the national and at the European level. In March 2019, the EU adopted a regulation establishing a framework for the screening of FDI into the Union. It pursues the goal of coordinating investment screening policies of the member states and to defining criteria based on which they can block FDI due to security and public order concerns in areas such as critical technologies and critical infrastructure. Rapidly rising levels and the strategic nature of Chinese investment in EU member states in the first half of the 2010s until 2016 triggered this legislative change (Schild and Schmidt 2024, 95-105). The EU's investment screening framework regulation serves the purpose of coordinating member states' investment screening policies. Thereby, the European Union enlarged

1 I would like to thank Carolyn M. Dudek and Eugénia da Conceição-Heldt for their helpful comments on earlier versions of this paper.

2 Drei Fragen an Annalena Baerbock. In: Internationale Politik Mai-Juni 2022, p. 8 (my translation).

its toolbox to deal with the challenge represented by the Chinese non-market economy and its authoritarian state, ever more repressive internally and ever more assertive externally. Does this policy change reflect domestic demands for protectionism from private actors and/or policy-makers' changing perceptions of longer-term European economic interests when facing stiffer high-tech competition from a rising economy moving up the value chain and improving its position in the international division of labour? Or did policy-makers' perceptions of security risks and challenges emanating from Chinese investments, notably from state-owned enterprises (SOEs), drive this policy change? To put it differently: Can we interpret reforms of inbound investment screening as a case of a declining economic power turning towards economic nationalism and protectionism when facing a dynamic rising economic power (Flaherty 2023)? Or is the observable change rather an instance of a geopoliticization of the bilateral relationship with security concerns gaining in importance and potentially relative to economic interest?

As there is a bidirectional interaction between policy change at the national and at the European level, the paper does not only consider EU-level policy change. Germany, a key destination of surging Chinese FDI in the EU between 2010 and 2016, had a pivotal role as an agenda setter and driver of this EU policy change. Hence, the paper puts a special emphasis on disentangling economic and security interests as explanatory factors accounting for preference formation of the German federal government and the changes in national-level law and practice of FDI screening.

The paper draws on newspaper articles, policy papers, official documents, interest group position papers, and on the growing body of academic IPE and European studies literature on investment screening (e.g. Babic and Dixon 2022; Bauerle Danzman and Meunier 2023; Bourgeois 2020; Chaisse 2019; Chan and Meunier 2022; Grieger 2017; Lenihan 2018; Schill 2019). It contributes to this growing body of literature on FDI screening in the EU by analysing the weight of economic and security interests underlying this policy change. It reflects on the observable implications of economic and security interests as drivers of reform and elaborates a set of criteria for a fine-grained assessment of their relative importance, as they are by no means mutually exclusive. In doing so, it also contributes to the literature on the geopoliticization of EU trade policy (Defraigne 2017; Le Corré and Sepulchre 2016; Lai 2021; Meunier and Nicolaïdis 2019).

The empirical record indeed points to the growing weight of geopolitical and security interests as drivers of both European legal reforms and national German screening practices. There is a broad overlap between security interests with longer-term strategic economic interests as defined by policy-makers, as the latter tend to widen the scope of security interests beyond traditional national security objectives towards a broader understanding of economic security. There is little evidence, however, regarding private interest groups influencing the FDI screening based on their commercial interest towards a more protectionist approach.

The paper proceeds as follows. The next section develops hypotheses regarding economic and geopolitical interests as explanatory factors accounting for FDI screening law and practice and clarifies the empirical implications of a geopolitical turn of investment policy. Which empirical indicators would support an interpretation of a geopoliticization of the EU's investment screening policy, and which observable implications would rather point to a narrower economic rationale of policy change? The empirical sections first look at the agenda setting and the drivers of policy change at the European level and then at some examples of screening decisions in Germany, which can shed some light on underlying rationales of investment screening and national-level legislative changes in this policy field. The last section concludes.

## Geopoliticization of investment policy?

The extant IPE literature points to different explanatory factors accounting for FDI related policies in general and investment screening in particular. Chan and Meunier (2022) provide empirical evidence for an economic explanation of national preferences among EU member states for FDI screening. The higher the technological level of a country, the higher the concern of its government regarding the loss and transfer of technology to a competitor who does not display the same degree of openness to inbound FDI, notably in areas of strategic technologies. Chilton et al. (2020) showed that reciprocity concerns can influence public opinion and trigger opposition to the acquisition of domestic companies by entities from other countries that are less open to FDI. Babic and Dixon (2022) traced a process of incremental ideational change of governments in the UK and Germany accounting for a shift from a liberal approach to attract FDI towards a growing emphasis on national security, leading in turn to stricter investment screening. Roberts et al. (2023, 660) interpreted the spread and strengthening of FDI investment screening rules as being an instance of the effort to 'recalibrate the relationship between economics and security'. In a similar vein, Le Corre and Sepulchre (2016) and Defraigne (2017) saw the spread of stricter rules on investment screening as a consequence of rising geopolitical tensions and rivalry. In an explicitly realist perspective, Lenihan (2018) analyses investment screening as a tool of statecraft to defend or improve one's own economic and military capabilities to internally balance potential external threats. Investment screening is thus part of a longer-term national security policy. Lai (2021) stressed that 'most countries' FDI policies are vague and ambiguous, particularly when it comes to national security' because this ambiguity serves policy-makers to advance their political and commercial interests (Lai 2021, 497).[3]

Realists tend to stress the importance of economic resources for security provision. According to Kirshner (1998, 66), 'it is difficult to disentangle the political and economic objectives of states' as there is an 'underlying long-run harmony between the national pursuit of wealth and power', the two being deeply enmeshed. Gilpin sees security and economic welfare interest not in terms of a 'hierarchy of goals, with its associated emphasis on maximization' and refers instead to an indifference analysis, which 'assumes individuals make trade-offs among these objectives and pursue "satisficing" strategies [in the sense of Herbert Simon, J. S.] rather than maximising strategies (…). That is to say, an individual [or a state] will not seek to achieve one objective at the sacrifice of all others but will seek an optimum position on the set of indifference curves' (Gilpin 1981, 20). Even though 'power' and 'plenty' are by no means contradictory goals, the relative importance of security and economic objectives can change over time. In the short run, security and economic objectives might also stand in opposition to each other.

Do we find evidence for a process of geopoliticization characterized by an increasing emphasis on security and geopolitics? Meunier and Mickus define geopoliticization as the 'reframing of a policy issue as a geopolitical problem' (Meunier and Mickus 2020, 1081). Meunier and Nicolaïdis (2019, 107) refer to geopoliticization as 'the external face of economic statecraft whereby trade policies come to be embedded in power rivalries'. Security interests gain in importance when evaluating investment relations with other countries. A geopolitical framing implies that policy-makers distinguish between different countries of origin of inbound FDI investment as some countries are different, China being one of them (Meunier 2014a).

The process of geopoliticization entails a growing weight of security objectives in investment screening policies. Geopolitical security concerns can take different forms. A growing concern of policy-makers with relative instead of absolute welfare gains from economic exchange would clearly indicate a framing of the bilateral economic and investment relations in terms of a longer-term power struggle. Furthermore, security concerns could relate to the capacity of the other side to weaponize economic interdependence and to cause disruptive shocks, using economic means to pursue geopolitical ends (Farrell and Newman 2019; Drezner et al. 2021). Geopoliticization of a bilateral investment relationship not only entails its reframing as a geopolitical problem; it also entails the politicization of investment screening cases and decisions.

[3] For a similar argument, see Bian (2021, 570).

This implies a higher public visibility, a higher degree of controversy surrounding the issue and a growing number of actors taking part in the debate (Grande and Hutter 2016).

How, then, can we disentangle economic from security concerns and interests when trying to identify key explanatory factors driving policy change? Which are the empirically observable implications of a geopoliticization of FDI screening? The following indicators can be used to identify the importance given in this trade-off between economic and security goals to geopolitical compared to economic interests as drivers of policy change in the EU's policy on the screening of inbound FDI.

*First*, the reframing of investment relations and FDI as a geopolitical concern should be embedded in and preceded by a broader process of geopolitical reframing of economic relations specifically with China, seen as being different from the rest of the world. *Second*, the agenda for policy change should be set not by private economic actors and their interest groups asking for protection from rival foreign companies but rather by public actors pursuing security goals. *Third*, agenda setting by actors from directly security-related ministries, such as defence and home affairs, and the related policy networks and not (only) by actors from ministries for the economy and finance would provide even more convincing empirical evidence regarding the underlying geopolitical interests and concerns.

*Fourth*, do actors advocating FDI screening articulate security concerns when providing a rationale for legislative change? Of course, security-related arguments might only provide a smokescreen to hide economic interests, as material interests might be considered less defensible than security interests for either political or legal reasons. Therefore, we look, *fifth*, at how broadly security interests are defined. Genuine security concerns can translate into a broad definition of security and of criteria used to vet investments. However, a long and vague list of security concerns and related criteria used to vet FDI, including all sorts of cutting-edge technologies, would be compatible with an interpretation that sees security concerns merely used as a pretext to advocate protectionist policies to prevent rival firms from acquiring valuable assets and technology. A short and precise list closely related to narrower national security concerns, protecting producers of armaments and dual-use goods and prohibiting the acquisition of critical infrastructure, would contradict an economic interest interpretation.

*Sixth*, do we observe a changing time horizon of decision-makers, emphasizing long-term economic and security implications of Chinese FDI more than short-term economic gains? According to Meunier (2019, 355) '[t]he main concerns [in Europe] are less about direct threats to national security than about the long-term implications for the economic competitiveness of the host country if China acquires technology'. Is a link being made between longer-term competitive disadvantages of a continuing sell-out of valuable European assets to Chinese companies and Chinese material power resources that the party state might use against the EU and its security interests? *Seventh*, particular security concerns triggered by FDI coming from Chinese state-owned or controlled enterprises would provide evidence for a geopolitical logic of FDI screening.

These indicators mainly relate to agenda setting, political legitimation of policy changes, and the concrete content of legislation in terms of criteria for evaluating and potentially blocking FDIs. Beyond this, we can analyse how individual EU member states use their national FDI screening mechanisms. The European and national-level screening legislation provides a legal framework and a toolbox. When making use of this toolbox, member states can define the trade-off between economic welfare and security objectives – that is the exact position on the indifference curve –in manifold ways and can change their optimum position on it over time.

*Eighth,* blocking of investment with a clear link to the production of defence-related and dual use goods and to critical infrastructure the control of which might provide the Chinese party-state with an option to use geo-economic strategies with the potential to cause heavy disruptions and economic havoc would support the hypothesis of a growing geopoliticization of FDI screening practices.

The politicization dimension of the geopoliticization of investment relations can be assessed by looking at the salience of EU-Chinese investment relations in general and the level of controversies regarding specific cases of mergers and acquisitions in particular. *Ninth*, Chinese FDIs and the European regulatory responses gaining political salience beyond the narrow policy networks dealing with investment relations would be indicative of geopolitization.

## Geopoliticization of problem framing

When comparing basic policy documents on the EU's strategic relationship to China over time, a change in the broader discourse on economic relations with China is all too obvious. In their joint communication to the European Parliament, the European Council and the Council of March 2019, the Commission and the EU's High Representative for Foreign Affairs and Security Policy dealt with China as being 'simultaneously, in different policy areas, a cooperation partner with whom the EU has closely aligned objectives, a negotiating partner with whom the EU needs to find a balance of interests, an economic competitor in the pursuit of technological leadership, and a systemic rival promoting alternative models of governance' (European Commission/High Representative 2019, 2).

Whereas earlier policy papers from the 1990s and early 2000s stressed the potential of the partnership, the latest 'strategic outlook' from 2019 bluntly stated that 'there is a growing appreciation in Europe that the balance of challenges and opportunities presented by China has shifted' (European Commission / High Representative 2019, 1). Geopolitical language has thus increasingly entered EU trade policy documents.

More than in the past, the EU stressed the 'well-understood self-interest' and the need 'to equip itself with tools to operate in a more hostile international environment if necessary'. '(B)uilding a fairer and rules-based economic relationship with China is a priority' (European Commission 2021b, 4, 8, 9). The perception that the EU is dealing with a competitor pursuing a geo-economic strategy has indeed gained ground.

Alongside the references to unfair trade practices and the lack of reciprocity in trade and investment relations, the self-description of the EU's trade policy as pursuing 'a further EU policy shift towards a more realistic, assertive, and multi-faceted approach' (European Commission / High Representative 2019, 1) also gained in importance. In its 2019 strategic outlook, the Commission and the High Representative treated China for the first time as a potential security threat for the EU and not only as a potential partner for dealing with security challenges in other parts of the world. This security threat perception related to Chinese investments in areas of critical infrastructure 'such as 5G networks that will be essential for our future and need to be fully secure' (European Commission/High Representative 2019, 9). Furthermore, the document stressed the security threat the EU faces from the Chinese military build-up:

> China's increasing military capabilities coupled with its comprehensive vision and ambition to have the technologically most advanced armed forces by 2050 present security issues for the EU, already in a short to mid-term perspective. Cross-sectoral hybrid threats including information operations, and large military exercises not only undermine trust, but also challenge the EU's security and must be addressed in the context of our mutual relationship' (European Commission / High Representative 2019, 4).

This provides an example for a long time horizon of European policy-makers dealing with the economic and security challenges emanating from China. The structural power shift towards China and its assertive geopolitical strategies fuel threat perceptions and security concerns in the EU. However, contrary to the US, security concerns do not provide the key lens through which EU-level policy-makers tend to analyse the EU's bilateral economic relation with China. The economic narrative regarding the unlevel playing field and calls for more reciprocity remains dominant compared to security-related problem perceptions in the EU institutions' discourses and policy documents on its bilateral relation with China (Schild and Schmidt, 2024; 70-81).

To sum up: There is evidence of clearly growing, albeit still of limited importance, geopolitical concerns and interests compared to economic concerns and evidence for a longer time horizon of EU policy-makers when defining the strategic relationship with China. This provides fertile ground for a geopoliticization of investment related policies.

## Agenda Setting

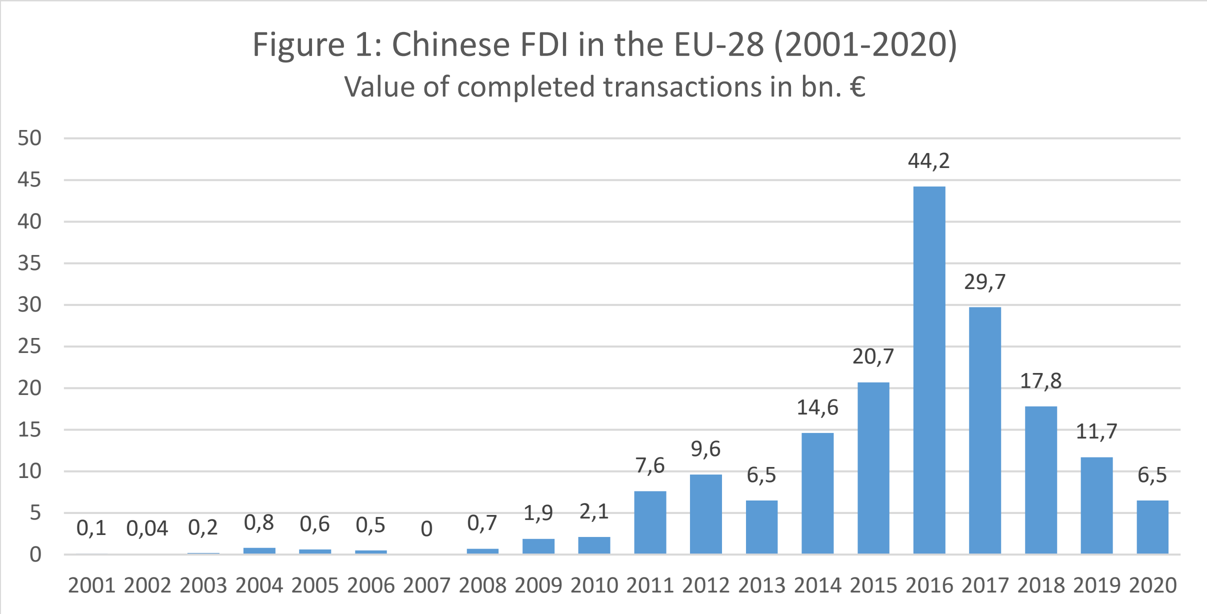
Before adopting the investment screening framework regulation in 2019, the EU had no European-level regime for vetting inbound FDI. The national regimes on investment screening (as far as they existed) differed substantially and legal fragmentation prevailed. With the entry into force of the Lisbon Treaty, FDI became part of the common commercial policy, so that the EU gained exclusive competence in this field and was empowered to regulate inbound direct investment, with the exception of portfolio investments (Article 207 TFEU).

Towards the end of the 2000s, a debate emerged on potential dangers of FDI, in particular regarding the role of sovereign funds, and on the need for EU-level rules (Grieger 2017, 11). However, it was not until the mid-2010s that Chinese foreign direct investment (FDI) into Europe became a salient issue. The very low level of stocks and flows from China to the EU (see graph 3) until the late 2000s explains the low salience before the 2010s. Things changed quickly thereafter. Highly dynamic growth—an eighteen-fold increase of Chinese FDI in the EU between 2010 and 2016, combined with the strategic choice of Chinese investments changed perceptions. Chinese FDI increasingly took the form of mergers and acquisitions (M&A) rather than greenfield investments, which were initially more important. The former provide Chinese companies with access to European technologies, skills, and equipment instead of transferring technology from China to the EU.[4] In 2016, the peak year of Chinese FDI in the EU, the acquisition of advanced manufacturing companies accounted for a third of all Chinese investments in value (Hanemann and Huotari 2017, 5). In Germany, the value of Chinese FDI investments rose steeply from 2015 to 2016 (Meunier 2019, 347). The strong FDI increase from China until 2016, the strategic choice of targets and a number of particularly controversial company takeover bids in critical infrastructure and cutting-edge technology companies such as robotics and the semiconductor industry in 2015 and 2016 sparked broader public debates and media attention. In Germany, the takeover of KUKU, world leader in robotics, by the Chinese Midea Group and China's Fujian Grand Chip Investment Fund takeover bid for chip equipment maker Aixtron, later dropped, provided policymakers with focusing events (see below), triggering demands for policy change and opening a policy window for new legislation on investment screening, both at the national and at the EU level.

Chinese FDIs in the EU, being part of a ‘strategy of aggressive investments into Europe’s high technology and infrastructure sectors’ (Godement 2020, 267), raised a

[4] On trends of Chinese FDI in Europe, see Hanemann et al. (2019).

few concerns. *First*, gaining control of critical network-based infrastructure (telecommunication, electricity, railways) might represent a security risk in times of rising geopolitical competition with China.




*Source: Kratz et al. (2021)*

*Second*, and more importantly, there was a growing awareness in the EU that these mergers and acquisitions were not market driven, but part of a national industrial policy strategy, the Made in China 2025 plan (Gottwald et al. 2019, 136-138). The stated goal of this policy is to move Chinese companies up the value chain and to create national champions able to gain substantial world market shares, outcompeting their European rivals. The Commission saw 74% of the Chinese M&A deals in the EU since 2013 as being linked to the 'Made in China 2025' strategy (European Commission 2021a, 44). In some member states, the acquisition of high-tech crown jewels by Chinese companies sparked public controversies, providing evidence for a politicization of FDI (see below).

*Third*, Chinese investment in critical infrastructure and dual-use technology that might be used for armament production raised geopolitical and security concerns. Against the background of the spike in high tech takeover bids in 2016 and the KUKA and Aixtron cases, the German minister for the economy, Sigmar Gabriel, called in an op-ed for new German and European instruments 'to protect security-relevant technologies'. Particular attention should be given to cases 'in which a state-dominated enterprise links the acquisition of technology to the expansion of its geopolitical power' (Gabriel 2016, my translation). In the past, German actors, both private and public, proved reluctant to support a supranational FDI screening regime that might endanger the access of its industry to the Chinese market. The change in Germany's position on investment screening had an important impact at the European level.

The idea of adopting an EU-level screening framework legislation only gathered momentum when three major members – France, Germany, and Italy – joined forces to set the agenda for EU-level legislation on investment screening in February 2017. In their common letter, the ministers for the economy, Michel Sapin, Brigitte Zypries, and Carlo Calenda warned of a 'possible sell-out of European expertise' in key sectors of technological competence to non-EU investors acquiring tech companies for strategic purposes without European companies being allowed reciprocal access to their home market.[5] They successfully launched a debate on EU policy options. At the same time, the presidential candidate Emmanuel Macron repeated long-standing French calls for reciprocity in EU-China economic relations and warned against a 'naïve' EU policy on China. In his election manifesto, he called for a European control mechanism to screen third country FDIs to protect strategic sectors of the economy (Macron 2017).

In a common non-paper from July 2017, France, Germany, and Italy explained their ideas in more detail[6] and in August 2017, the German minister for the economy, Brigitte Zypries, addressed a letter to Commission president Jean-Claude Juncker and exhorted the Commission to act. She pointed to the 'one-sided concentration of [Chinese] investments in industrial high tech and key technology companies with clear links to the China 2025 strategy adopted by the Chinese government' and underlined the investment restrictions in the Chinese market: 'Open markets cannot be a one-way street' (Zypries 2017, my translation).

The president of the Commission, Jean-Claude Juncker, took up the cause and announced a legislative proposal in his 2017 State of the Union address on 13 September 2017, published on the same day (Juncker 2017). This proposal took key points mentioned in the Franco-German-Italian paper on board. It limited its ambition to outlining a European legal framework, defining principles, and reporting obligations on national investment screening procedures, without attempting to shift decision-making powers to the European level.

The Commission's rather cautious approach reflects the constellation of actors and interests it faced. Germany, France, and Italy feared a sell-out of high-tech expertise to Chinese investors and a one-sided technology transfer to China. Chinese companies

5 The letter is documented on the website of the German Bundesministerium für Wirtschaft und Energie: Brigitte Zypries, Michel Sapin, Carlo Calenda: Schreiben an EU-Handelskommissarin Cecilia Malmström, Februar 2017, URLr: https://www.bmwi.de/Redaktion/DE/Downloads/S-T/schreiben-de-fr-it-an-malmstroem.pdf?__blob=publicationFile&v=5 (last accessed: 28.1.2022).

6 Governments of France, Germany and Italy: European investment policy: A common approach to investment control, 28 July 2017, available from: https://g8fip1kplyr33r3krz5b97d1-wpengine.netdna-ssl.com/wp-content/uploads/2017/08/170728_Investment-screening_non-paper.pdf (last accessed : 30.04.2019).

might acquire technological leadership in key sectors thanks to long-term industrial and technological policy strategies along the lines of the Made in China 2025 plan and thanks to abundant state subsidies. Moreover, their participation in or takeovers of companies in critical infrastructure, ports (e.g. Piraeus Port in Greece), airports, power grids and other network-based utilities, might represent a potential security threat. The advocates of change faced a coalition of northern European member states with liberal and anti-protectionist economic ideas and southern European member states, such as Greece, Portugal, and Spain, eager to attract Chinese infrastructure investments to overcome the economic hardship of the Eurozone crisis. Capital-importing southern countries wanted the EU to stay open to Chinese investments, some capital-exporting northern countries feared Chinese retaliation as a reaction to investment restrictions. The liberally minded UK also had reservations. Some governments were internally split between advocates of a regime of free capital movements and actors pursuing a security agenda.[7] Chan and Meunier (2022) explain the dividing lines between member states based on differences in their technological expertise. Member states with important high-tech sectors and important Chinese investments in high tech lent more support to the investment screening reform than countries with lower levels of technology.

What about the private sector? The agenda setting for investment screening and the political initiative for lawmaking in this field did not respond to societal demands of stakeholders in the private sector, articulated by business associations. It clearly emanated from the governments of three key member states. Back in 2008, BusinessEurope articulated 'concerns over proposals to create a Committee on Foreign Investment in the United States or CFIUS-type review procedure to vet foreign proposals for mergers and acquisitions' as it found no evidence of politically motivated investments in the context of debates on sovereign wealth fund investment (BusinessEurope 2008). A decade later, it warned 'that the door to protectionism should remain closed', while supporting a 'calibrated, risk-based approach that respects the balance between achieving legitimate security and public order objectives while maintaining an open and welcoming environment for much needed FDI in the EU' (BusinessEurope 2018, 1). Orgalim, a European-level federation representing Europe's technology industries and strong exporters—key targets of Chinese FDI in Europe—saw no 'need for a second layer of investment screening at European level'. It warned that the Commission 'underestimates the negative effects such a legislation would entail in the long run, namely an erosion of companies' freedom to invest in "critical

[7] For an overview on actors' interests and coalitions, see Rasmussen Global (2017, pp. 3-4).

technologies" such as robots, semiconductors, and dual-use goods, leading to an overall decrease of investments in such technologies' (Orgalim 2018, 1). Support for the proposal came from AEGIS Europe, primarily representing the interests of import-competing sectors. It stressed that 'industries are increasingly faced with third country government-led acquisitions that erode the integrity of European manufacturing capacity' (AEGIS 2018). The Federation of German Industries (BDI), on its part, had not asked for a change in national law, nor for an EU-level investment screening legislation. Quite to the contrary, it saw policy responses both at the German and the EU level as being 'politically motivated' and made clear that 'German industry rejects protectionist measures' infringing upon private property rights of company owners and on the freedom of contract. 'Threats to introduce restrictions on market access for foreign investments do not qualify as suitable means to persuade China to open its markets' (BDI 2018). While in principle supporting the investment screening on security and public order grounds, it came out strongly against an ever greater acceptance of these concerns, repeatedly warned against a 'global spiral of investment protectionism' and rejected the use of investment screening as a tool of industrial policy and as a protective shield for European high-tech firms (BDI 2020). Whereas the BDI fully supports the EU's reciprocity discourse and demands in trade, 'German industry rejects reciprocity in the context of direct investments' (BDI 2018). Other important economic interest groups such as the Verband Deutscher Maschinen- und Anlagenbau-VDMA (Association of the Mechanical Engineering Industry with more than 3,400 members) and the Deutscher Industrie- und Handelskammertag-DIHK (Association of German Chambers of Industry and Commerce) published similar sceptical statements. Target companies of Chinese takeover bids did not ask for protection either. In the case of the KUKA takeover by the Chinese Midea group, KUKA's chief executive, Till Reuter, publicly supported the offer, contrary to the workers' representatives on its supervisory board (Chazan 2016; Reuters 2016). The investment screening proposal found support, however, from the Deutsche Schutzvereinigung für Wertpapierbesitz-DSW, Germany's leading association for private investors with some 30,000 members (Tan 2021, 37-39).

Executive autonomy from private interests proved to be high. On the national level, governments developed their preferences independently and even in opposition to key interest groups. Germany is a case in point, as the government's preference change on the topic stood in clear contrast to the position of the most powerful domestic business interest group, the BDI. Longer-term concerns regarding unfair high-tech competition with China and geopolitical security concerns trumped shorter-term business interests.

Economic interest motivated the scepticism about and opposition to EU-level investment screening in southern European member states such as Greece and Portugal, beneficiaries of Chinese direct investment in infrastructure, and in states serving as intermediaries for third country investments, such as Cyprus, Ireland, and

Luxemburg. Liberal, anti-protectionist member states such as Estonia, Finland, the Netherlands, and Sweden opposed the coming EU legislation on ideological grounds (Chan and Meunier 2022, 528).

What about security concerns? How did they influence the agenda setting process? Policy-makers repeatedly invoked security and public order concerns to justify the need for EU-level investment screening legislation. However, they might simply have used these arguments as a smokescreen to hide other concerns, notably protectionist interests in preserving high-tech expertise and brands from being sold out to China. From a legal point of view, security and public order concerns provide the only valid reasons allowing for a restriction of the freedom of capital movement as enshrined in EU primary law.[8] Therefore, it does not come as a big surprise that security concerns figured prominently in policy-makers statements and the Commission's legislative proposal's explanatory memorandum. A conceptual stretching of the notion of 'critical infrastructure' to cover many economic sectors, notably high-tech sectors and advanced manufacturing, might follow the same logic of disguising underlying economic interests in protection from current and future Chinese competitors. Furthermore, the French and German ministers for the economy, Le Maire and Altmaier, spelled out an economic rationale for using the investment screening instrument in their *Franco-German Manifesto for a European industrial policy fit for the 21st Century*: The investment screening framework 'needs to actually be used by Member States to protect Europe's strategic technologies and assets which are critical' (Bundesministerium für Wirtschaft und Energie and Ministère de l'Économie et des Finances 2019).

## Criteria for vetting inbound FDI

The FDI screening regulation adopted in February 2019 establishes a cooperation mechanism, both between the member states themselves and between the member states and the Commission, for screening direct investments that could endanger security and public order.[9] The regulation provides a long, non-exhaustive list of criteria based on which competent authorities can screen third country FDI. However, these criteria remain clearly linked to grounds of security and public order (Article 1(1)), which were never clearly defined. The only grounds referred to in the Union's primary law justifying restricting the freedom of capital movement are public security and public policy (Article 65(1)(b). The Commission sees the concepts of *security and public order*,

8 Articles 63 and 206 TFEU.

9 Portfolio investment is not covered by the regulation, see Regulation (EU) 2019/452 of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union, recital 9.

the latter not to be found in the treaties, and *public security and public policy* to be equivalent (Verellen 2021, 24). So far, the European Court of Justice has not provided a clear definition of public security and public policy. However, it opted for a restricted interpretation of their meaning, as there must be a 'genuine and sufficiently serious threat to a fundamental interest of society'.[10] Furthermore, it 'has ruled that purely economic and administrative grounds cannot be accepted as grounds to restrict free movement' (Zwartkruis and de Jong 2020, 457). Therefore, competitive distortions due to public subsidies or general reciprocity demands, as mentioned in the Franco-German-Italian non-paper, did not find their way into the regulation, which sticks to a predefined legal path.

The regulation defines a comprehensive list of factors that member states can use to check third country FDI projects with regard to their impact on security and public order. This encompasses the FDIs impact on critical infrastructures, 'including energy, transport, water, health, communications, media, data processing or storage, aerospace, defence, electoral or financial infrastructure, and sensitive facilities, as well as land and real estate crucial for the use of such infrastructure' (Article 4(1a)), on critical technologies and dual- use items, 'including artificial intelligence, robotics, semiconductors, cybersecurity, aerospace, defence, energy storage, quantum, and nuclear technologies as well as nanotechnologies and biotechnologies' (Article 4(1b)), on supply of critical inputs such as raw materials and energy (Article 4(1c), on 'access to sensitive information, including personal data, or the ability to control such information' (Article 4(1d)), and finally, on 'the freedom and pluralism of the media' (Article 4(1e)).

This long list of areas and types of investments that member states can take into account when vetting inbound FDI indeed covers security-related fields both in the narrower sense of dual-use technologies with evident military uses such as aerospace, defence and nuclear technologies and in the equally security sensitive field of critical infrastructures, the control of which can be abused to cause deep disruptions in the economy and society of host states. As the regulation covers broad areas of cutting-edge technologies from quantum computing and artificial intelligence to energy storage, nano- and biotechnologies, the list is nevertheless fully compatible with an economic interest interpretation of the underlying driving forces.

Concerns about data privacy, electoral infrastructure and the freedom and pluralism of the media can hardly be considered as addressing narrower security interests but rather the defence of a democratic model of individual rights and public freedom and

[10] ECJ C-54/99 (Église de Scientology), para 17, quoted after Zwartkruis and de Jong (2022).

the integrity and proper functioning of the democratic process. As they address concerns about European autonomy and sovereignty, they can be considered geopolitical in nature. They are clearly not based on economic interests.

The screening procedure should consider whether the investor is directly or indirectly controlled by a government or a state body (Article 4(2a). Here, the shadow of Chinese state-owned enterprises or undertakings with close links to the party state looms large. This provides us with evidence of a geopoliticization process, as it singles out a particular type of investor that might weaponize economic interdependence to pursue geo-economic strategies serving political goals.

## Practices of investment screening: the German case

A look at the practice of national investment screening lends support to the assumption that security interests played an increasing role in beefing up investment screening, both at the national and European level. Security interests regarding Chinese FDI relate to a) gaining control over strategic assets and critical infrastructure (e.g. power plants and grids, ports, railway networks) that might be used for acts of sabotage and disruption; b) acquisition of dual-use technology for military build-up (e.g. semiconductors, optical equipment); c) the transfer to of technical know-how and armament-related technology to hostile third countries (e.g. North Korea) (Grieger 2017, 5).

Until 2014, no member state had ever blocked Chinese FDI based on its national investment screening regulations (Meunier 2014b, 1012). This changed quickly and profoundly thereafter. Germany, the second most important destination for Chinese FDI in the EU-28 after the UK, provides evidence for this change. Several German decisions on critical cases of Chinese takeover bids for companies testify to the rising importance of security concerns.[11]

In 2016, the Chinese state-owned National Chemical Corporation (ChemChina) acquired the prominent German machine manufacturer Krauss-Maffei, paying € 925 million, the highest amount up to this point (Der Spiegel 2016). This takeover increased awareness on the strategic nature of acquisitions by Chinese SOEs of German high-tech companies (Jungbluth 2018). The acquisition in 2016 of KUKA, a high-tech crown jewel of German industry and a world market leader in industrial robots, by the Chinese Midea Group offering € 4.5 billion sparked strong public controversy. After this 'landmark Chinese Midea acquisition of German Kuka Robotics (…) [a]cquisitions made by Chinese investors in German are covered by the media on a weekly basis, featuring examples of Chinese companies taking over German industrial leaders and national

[11] The following paragraph is based on overviews provided by Tan (2021, 34-36) and Bungenberg and Reinhold (2023, 9-18).

champions (…)' (Bian 2021, 572). The Kuka case provides evidence for a politicization of FDI, as it was seen as a sell-out of German high tech. The federal government hoped for an attractive counteroffer by a German company, which did not materialize. Based on a preliminary examination of the case, the federal ministry for the economy (BMWi) did not find sufficient evidence for a threat to German security and public order (Bungenberg and Rheinhold, 2023, 10).

Thereafter, Chinese investment in critical infrastructure and dual-use technology that might be used for armament production raised ever more geopolitical and security concerns. In the same year, 2016, China's Fujian Grand Chip Investment Fund made a € 670 million takeover bid for the systems manufacturer and chip equipment maker Aixtron and gained clearance after review from the BMWi. The Obama administration blocked the US related part of the takeover on security grounds following an investigation by CFIUS in December 2016 (FT.com 2016). Following the US decision, the German government changed its stance, and for the first time ever rescinded its previous approval and reopened the case. The Chinese company dropped its bid ahead of the BMWi's final decision (Bian 2021, 582).

When the State Grid Corporation of China (SGCC) announced a bid to acquire 20 % of the German high-voltage transmission grid company 50Hertz in 2018, the German government successfully used the public development bank Kreditanstalt für Wiederaufbau (KfW) as a 'white knight' to buy a 20 % share of 50Hertz sold by its former owner in order to block the Chinese participation in its capital. The German government chose this option as it could neither convince the Belgian Elia Group, the majority owner of 50Hertz, to durably increase its stake in the company, nor could it block the Chinese acquisition of 20 percent of 50Hertz's shares as the offer remained below the 25 percent threshold in force. This experience triggered a regulatory response, a change to the Foreign Trade and Payments Ordinance (Außenwirtschaftsverordnung-AWV)[12] in December 2018. It lowered the review threshold to 10 % for FDI in areas related to defence and security-relevant critical infrastructures (Bundesregierung 2018). In the process of interministerial coordination, the ministry of defence had called for this lower threshold.[13] 'Based on security considerations, the German government has a strong interest in protecting the German transmission grid as the core of the German energy supply and classifies the latter therefore as being a critical energy infrastructure' (Bundesregierung 2018, my translation). In 2017, another change of the AWV had already extended the list of security-relevant technologies under particular scrutiny.

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12 An English translation of the AWV is available at: https://www.bmwk.de/Redaktion/DE/Artikel/Aussenwirtschaft/investitionspruefung.html

13 Interview with a former high-ranking official of the German Ministry of Economics on 9 February 2022.

Against the background of the spike in high tech takeover bids in 2016 and the KUKA and Aixtron cases, the German minister for the economy, Sigmar Gabriel, called in an op-ed for new German and European instruments 'to protect security-relevant technologies'. Particular attention should be given to cases 'in which a state-dominated enterprise links the acquisition of technology to the expansion of its geopolitical power' (Gabriel 2016, my translation).

In 2018, the German federal government was poised to veto an attempt by the Chinese Yantai Taihai Corporation to take over the German Leifeld Metal Spinning, a leading tooling machines maker for metal forming, active in the automotive sector, aerospace, energy and nuclear industry. One day ahead of the federal government's cabinet meeting to discuss the matter, Yantai Taihai withdrew its offer. Once again, the government had security concerns as Leifeld technologies and products could be used for enriching uranium and in the aerospace industry and hence for military purposes besides civilian ones (Die Welt 2018; see also Bungenberg and Reinhold 2023, 12).

In 2020, security concerns motivated the federal government's first ever prohibition of a takeover. The state-owned China Aerospace and Industry Corporation tried to acquire IMST, a producer of satellites and radar technology and supplier of the German army, producing short-range and anti-aircraft missiles. In this case, the BMWi articulated strong security concerns and saw IMST technology belonging to the 'key know-how' for the German armament sector (Bungenberg and Reinhold 2023, 13, my translation). Also in 2020, the German government enlarged the circle of economic sectors subject to screenings of investments for security and public order to include the health sector (Bundesregierung 2020). In May, the 17$^{th}$ revision of the AWV added 16 specific security-relevant sectors (new paragraph 55a), reflecting critical technologies as mentioned in the EU framework regulation (additive manufacturing, aerospace, AI, autonomous driving and aviation, cyber security, quantum and nano technologies, robotics, satellite systems, semiconductors) and defined a 20 % threshold for triggering a review.

Two other government decisions prohibiting Chinese acquisitions came in November 2022 in the semiconductor industry. One prohibited the sale of the Elmos's semiconductor plant to Chinese-owned Silex Microsystems in order not to increase German dependence on semiconductor products from Chinese companies and thereby undermining the security of supply chains. The other blocked the acquisition of ERS electronics by a Chinese company on grounds of risk for security and public order. ERS electronics manufactures components for the production of silicon wafers (Chazan 2022). In July 2024, the ministry for the economy blocked the takeover of a branch of MAN Energy Solutions, a manufacturer of gas turbines, by the Chinese CSIC Longjiang GH Gas Turbine Co (GHGT). The federal government feared the use of the turbines to propel war ships, as GHGT belongs to the China State Shipbuilding Corp (CSSC), which constructs ships for the Chinese navy (Frankfurter Allgemeine Zeitung, 2024).

The most visible and highly controversial recent case of investment screening decisions came with the attempt by Chinese state-owned COSCO Shipping Ports Limited (CSPL), part of the COSCO Shipping Corporation (COSCO), to acquire a 35 % stake in the Container Terminal Tollerort GmbH (CTT) in Hamburg (Mardell and Giamello, 2021). This sparked a conflict inside the German federal government. No less than six ministries, among them defence, foreign affairs and interior, and intelligence agencies came out against the COSCO participation and raised security concerns, such as the risk of intelligence gathering,[14] and stressed the need to protect critical infrastructure (Chazan and Yang 2022). Chancellor Scholz, a former mayor of Hamburg with close ties to its business community, overruled them, however. The conflicting government actors were split mainly along party lines, the liberal FDP and the Greens adopting a much more cautious stance on China in general and this acquisition in particular, compared to the social democrats (SPD). The coalition parties were able to strike a compromise allowing for a COSCO stake in CTT up to the ceiling of 24.99 %, thus preventing veto rights and limiting COSCO's influence on CTT's business strategy (Jones 2022). According to the Green minister for the economy, Robert Habeck, investment screening is now 'embedded in a geopolitical context that is highly politicized" (Chazan 2022). In a similar vein, the Habeck ministry for the economy and energy stressed 'rising global geo-economic competition' in its explanatory part of the recent change to the German Foreign Trade and Payments Ordinance in 2021. 'Concrete investment projects serve increasingly broader political-strategic interest. An effective investment control instrument preserves the security interests of the Federal Republic of Germany' (Bundesministerium für Wirtschaft und Energie 2021).

These cases of investment screening illustrate the growing concerns of successive German governments regarding the security risks of Chinese investments in advanced German technology and critical infrastructures. This is also reflected in the increased number of reviews, which grew from 40-50 cases per year between 2009 and 2016 to a peak of 306 in 2022, with Chinese investors usually ranking third behind the US and the UK (Bungenberg and Reinhold 2023, 22; Bundesministerium für Wirtschaft und Klimaschutz 2024).

The successive and incremental changes to the AWG and AWV reflect a trend towards an ever more encompassing understanding of security beyond national security defined in military terms towards a broader conception of economic security.

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[14] A controlling stake in a part of the Hamburg port infrastructure might provide the Chinese state-owned company deep insights into the flow of goods and in commercial practices, similar to the 'panopticon effect' discussed by Farrell and Newman (2019), potentially allowing for the weaponization of economic interdependence by China.

Considering the cases subject to review, the emphasis put on security and public order can hardly be interpreted as being only a smokescreen behind which commercial interests lurk. They provide evidence for a growing willingness to reassess the trade-off between economic and commercial interests in attracting foreign capital on the one hand and security objectives on the other in favour of the latter.

## Discussion and Conclusion

Security concerns regarding inbound FDI from China have indeed grown in importance since the middle of the 2010s. A number of our indicators to assess a process of geopoliticization of investment screening can certainly be found. We see elements of a geopolitical framing of Chinese FDI by EU and national actors. The explicit warning of the former German minister for the economy, Sigmar Gabriel, about state-dominated Chinese enterprises acquiring advanced technology to expand China's geopolitical power is a case in point. The special concern regarding state-owned enterprises is reflected in the text of the EU's framework regulation as the screening procedure should consider whether the investor is directly or indirectly controlled by a government or a state body. This provides evidence for a geopoliticization process that singles out particular types of investors and countries that might weaponize economic interdependence when pursuing their geopolitical goals. Furthermore, this geopolitical framing of investment screening is embedded in a broader geopolitical discourse on EU-China economic relations. However, EU and national policy-makers do not adopt a strategic power competition perspective to interpret bilateral relations with China in a similar way to US administrations since the 2010s.

Agenda setting for policy change came from public, not private actors. Economic interest groups did not advocate a protectionist turn on investment screening but rather warned against rising protectionism. Among the public actors setting the agenda, ministers for the economy were key, not security related ministries such as defence or home affairs. This is not only due to their legal competence in investment screening reviews. Public statements of agenda setting by ministers for the economy reflect a growing concern about a sell-out of European cutting-edge technologies to Chinese companies that are moving up the value chain and could outcompete European companies in the latter's fields of excellence. By pushing for policy change, the French, German, and Italian governments prioritized longer-term protection of key high-tech industries and longer-term economic interests over the short-term interest of cash-strapped European companies interested in Chinese investments. This reflects a longer time horizon of policy-makers compared to shorter-term business interests. Initially, geopolitical concerns played a minor role in their discourse. For legal reasons, however, EU-level and national policy-makers had to refer to security and public order concerns as they provide, according to European primary law, the only justification to limit freedom of capital movements. Over time, policy-makers more regularly made reference to geopolitical concerns regarding Chinese (public) investments in European high tech and critical infrastructure.

The criteria defined in the EU's investment screening regulation do not reflect a narrow security concern. They certainly address security risks, notably regarding the control of critical infrastructures and dual-use goods. However, they are quite broadly defined, covering large fields of high-tech sectors. Of course, this could be interpreted as flowing from longer-term concerns about rising Chinese economic power resources to which investment in European high-tech industries can contribute. They are rarely invoked as explicitly as in the European Commission and HR's strategic outlook on EU-China relations (European Commission and High Representative 2019).

Looking at the German implementation of investment screening, we find several cases of investment screening pointing to security concerns. This holds true for the indirectly blocked investment in the German high-voltage electricity grid and for the blocked investment in the closely defence-related technology company IMST. On the other hand, the blocked Aixtron takeover provides us with a case of a company producing dual-use semiconductor technology in which the Obama administration rang the alarm bell, not the German government. This example provides us with evidence of the higher importance attached to security interests by the US compared to EU member states' governments.

Inbound FDI, investment screening and legislative changes thereto usually do not spark broader interest beyond narrow policy-maker networks. The KUKA robotics producer takeover by the Chinese Midea group provides us with a first example of high politicization, that is high salience, media interest and public controversy. It was a game changer, a 'wake-up call that turned the tide on the discussion of strategic CSIL [Chinese state-led investments, J.S.] in Germany' (Babic and Dixon 2022, 129). It contributed to turning the German government into an advocate of EU-level legislation on investment screening. The heated German debate about COSCO's participation in the Port of Hamburg in 2022 showed that the likelihood of particular takeover bids being highly politicized is clearly growing.

Table 1 summarizes the key findings of this paper. Overall, a mixed picture emerges. We find clear evidence that geopolitical concerns and security interests gained in importance and provided a rationale for policy change both on the European and the national level. The longer-term concerns of the governments most actively pushing for EU legislation on investment screening revolved more around economic long-term interests and were rarely framed in global power struggle language as they routinely are in the US. Security concerns in Europe are more narrowly focused on the disruptive potential of Chinese investments in critical infrastructure and with a direct military use of cutting-edge and dual-use technologies, less so with the long-term Chinese economic benefit flowing from investments in EU member states that could strengthen the resource base of China's military build-up and geopolitical strategy.

*Table 1: Indicators of a geopoliticization of Chinese FDIs in the EU: Empirical evidence*

| **Indicator** | Confirmed? |
|---|---|
| 1. Geopolitical framing of EU-China investment relations embedded in and preceded by broader geopolitical framing of EU-China economic relations. | Yes |
| 2. Agenda setting by public, not by private actors. | Yes |
| 3. Agenda setting by security-related institutions / ministries | No |
| 4. Decision-makers articulate security concerns in order to make the case for investment screening. | Yes |
| 5. Criteria used to evaluate and vet investments are well defined, concise and narrowly security-related. | No, broad range of criteria |
| 6. Time horizons of decision-makers are getting longer as longer-term power resources implications of FDI gain in importance. | Yes |
| 7. FDI by Chinese state-owned or controlled enterprises raise particular security concerns. | Yes |
| 8. Decisions to block Chinese FDI mainly relate to the defence sector, dual use goods and critical infrastructures. | Yes, in the German case |
| 9. Chinese FDIs and the European regulatory response to them gain political salience beyond the narrow policy networks dealing with investment relations. | Individual cases of high salience (KUKA) |

*Source*: Own compilation.

The EU has not fully replaced its mainly liberal economic paradigm for assessing the costs and benefits of economic and investment relations with China with a realist geopolitical paradigm. We rather see a layering of geopolitical frames and interests onto the liberal paradigm and the addition of instruments of economic security provision to the EU's toolbox. The new legal framework on FDI screening at the European level and the legislative changes triggered in a growing a number of member states, however, provide a solid legal basis for a more frequent use of FDI screening to achieve security objectives. The increasingly frequent use made of FDI screening legislation invoking security concerns by the German government provides evidence for a longer-term readjustment of the security-welfare trade-off in favour of security objectives. This supports a realist interpretation of the drivers of policy change, as the rise of China and its FDI strategies are increasingly perceived as a potential security threat, not merely as an economic challenge.

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