Foreign investment in Europe

Capital control

Chinese buyers of infrastructure and technology firms face more scrutiny

"WE ARE not naive free traders. Europe must always defend its strategic interests," said Jean-Claude Juncker, the president of the European Commission, last year as he introduced plans to screen foreign investment into the European Union. America has had such rules since the 1970s; they are set to tighten further. The EU used to be more relaxed about acquisitions by foreigners. Now it too is toughening up.

The target is China, whose firms have been on a shopping spree (see chart). Purchases of fripperies such as football clubs and hotels have been curbed by the Chinese authorities, but investment continues to flow into technology and infrastructure, notes James Zhan of the UN Conference on Trade and Development (UNCTAD).

Several European countries, including Germany and Italy, have extended investment-screening rules beyond energy and transport infrastructure to cover technology deemed important for public security, for example in telecoms. Chinese involvement in building Hinkley Point C, a nuclear-power plant, led Britain to tighten its rules. Last month France's government blocked the sale of its share of Toulouse airport to a Chinese consortium, which would have gained a majority stake.

European lawmakers suspect that purchases by private Chinese investors are an extension of their government's "Made in China 2025" strategy, which aims at overtaking Western innovation, says Franck Proust, a French member of the European Parliament. Attitudes have soured most in Germany. A turning-point came in 2016,

Buying time

Chinese FDI* flows into the European Union, $bn

Source: Rhodium Group *Foreign direct investment

says Cora Jungbluth of Bertelsmann Stiftung, a think-tank, when a Chinese firm acquired KUKA, a German robotics firm, for €4.5bn ($5bn). Critics fumed that, even as Chinese companies gained Western know-how, German ones were facing discrimination in China. Last year Germany, with France and Italy, pushed for an EU-wide regime that could block acquisitions in sectors where European firms did not have reciprocal access in China.

Mr Juncker's proposals, which are now before the European Parliament, are more timid. They allow the commission to issue non-binding opinions on foreign acquisitions, and encourage EU members to share information on the possible effect on public security. They represent progress, says Mr Proust, considering that more than half of EU members do not even have a framework in place to assess such deals. But he would prefer something harder-edged.

Not every EU member feels this way. China's Belt and Road Initiative, which involves it underwriting billions of dollars of infrastructure investment along the old Silk Road linking it with Europe, is regarded by some southern and central European countries as a source of much-needed investment. Other EU countries worry that such eagerness could be exploited to divide the continent. Awkwardly, austerity measures imposed as a condition of bailouts during the euro crisis contributed to Chinese influence. Privatisations intended to help stabilise wobbly public finances mean that the Chinese state now controls Piraeus, a Greek port, and owns the largest stake in Portugal's electricity grid.

The Nordic countries and the Netherlands meanwhile argue that stricter rules on Chinese investment could inflame trade tensions, even as the global trade environment worsens. Business groups fear that tighter screening could be used as a cover for protectionism. International organisations, including UNCTAD, warn that it could scare off investors and harm economic growth. A less starry-eyed approach to foreign investment brings risks, too. ■

Financial regulation

Green tape

The European Union wants to make finance more environmentally friendly

TO GAUGE an issue's importance, a guest list is a good place to start. The one for a conference in Brussels on March 22nd to discuss the European Union's "action plan" on sustainable finance features heavy-hitters including Emmanuel Macron, France's president, and Michael Bloomberg, a former mayor of New York who campaigns on climate change. Given that sustainable finance is well-established, what action does the EU think is needed?

Investing with an eye to environmental or social issues, not just financial returns, has become mainstream in the past decade. According to the Global Sustainable Investment Alliance (GSIA), $23trn, or 26% of all assets under management in 2016, were in "socially responsible investments" that take account of environmental, social and governance (ESG) issues. New asset classes have sprung up. According to SEB, a Swedish bank, the issuance of green bonds, the proceeds of which are invested in environmental projects, reached $163bn in 2017, up from less than $500m in 2008.

Yet standards are a hodgepodge. Many certification and evaluation tools cover just one asset class; competing methodologies abound. It is here that the European Commission, and an advisory group of experts, sees a role for public policy. One aim is to create a framework within which to classify the sorts of activities that qualify as sustainable investments, and against which to benchmark existing standards. The commission proposes setting up an EU labelling scheme for green bonds.

It also plans to draft a law by mid-2018 to require all asset managers to consider ESG factors when giving advice, and to explain how they are doing so to their investors. The European Fund and Asset Management Association, an industry group, worries that this would turn ESG investing into a box-ticking exercise. But Christian Thimann of AXA, an insurer, and the chair of the expert group, argues that many financial firms still ignore clients' environmental or social preferences. Compelling them to tick boxes would be better than nothing, he thinks.

Another of the proposals has drawn fiercer criticism: to loosen capital requirements for banks' green investments. That goes against a decade's worth of financial regulation, which has sought to bolster banks' capital buffers. Even the commission's expert group seems dubious, writing that the proposal does not "seem to be quantitatively grounded". (The commission insists any changes will take financial stability into account.)

However the debate on capital requirements is resolved, the commission's plans look likely to boost sustainable finance in Europe. That will not turn the global financial system green on its own. But it will show how financial rules can be harnessed for environmental ends.