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The EU–China Comprehensive Agreement on Investment

THE ISSUE

On December 30, 2020, the European Union and China concluded in principle the Comprehensive Agreement on Investment (CAI). Beijing's sudden flexibility on the terms of the bilateral investment agreement is clearly part of an effort to preempt improving U.S.–EU relations. Essentially, the CAI gives European investors additional market access in China in exchange for access to markets that are already more open to China than China is to the EU. The deal will be a political win for China at a time when China's diplomatic relationships around the world are worsening. Beijing has become increasingly belligerent toward countries that want greater transparency in areas like the use of forced labor and the origins of COVID-19.

The U.S. and the EU must work together to address the China challenge. With the CAI, Europe is making a down payment on a separate peace that will do long-term damage to the transatlantic relationship.

WHAT IS THE EU–CHINA COMPREHENSIVE AGREEMENT ON INVESTMENT?

- The EU–China CAI is a bilateral investment treaty that has been concluded in principle between the members of the EU and China. A finalization and ratification phase involving Brussels and member capitals will last at least a year.
- European and Chinese officials began negotiating the deal in 2014. In April 2019, both sides agreed to try to conclude CAI negotiations by the end of 2020.
- European negotiators secured market-access commitments from China in areas ranging from health services and chemicals to electric vehicles and telecoms. The agreement also aims to lift Chinese joint-venture requirements in sectors like automobiles and financial services; to increase legal protections for investments; to establish a fair investment environment against Chinese state-supported industries; and to increase transparency in China's regulatory environment.
- In some of these very specific cases, the Chinese may uphold their commitments. They have done so before. Where the commitments are more vague and without deadlines, involving international labor standards and state-owned enterprises, for instance, the prospects are highly questionable.
- In exchange for these concessions, the CAI offers the Chinese greater investment access to the EU in energy and manufacturing and makes assurances over existing access to EU markets.

DOES THE CAI HELP EUROPE?

- The EU is already a significant investor in China. Europeans have invested as much as $181 billion in China, Germany being the largest investor.
- A 2017 study suggested that the agreement could increase EU foreign direct investment (FDI) stock in China by as much as 0.6 percent to 1.9 percent, and increase Chinese FDI stock in the EU by as much as 0.3 percent to 0.9 percent.
- The CAI may also help European investors who are worried about competing with American investors after the U.S.–China Phase One agreement gave American investors certain protections as well as market access.

DOES THE CAI HELP CHINA?

- The CAI would be a big political win for Beijing at a time when there are increasingly negative views of China for its use of forced labor and its role in the origin and spread of COVID-19.
- China is increasingly dependent on foreign investment to support its industrial development by importing innovation and talent.
- China has already relaxed some of its investment restrictions over the past few years, including introducing a new foreign investment security law and decreasing the restrictions on its foreign investment negative list.
- Much like in the deceased U.S.–China bilateral investment treaty, China will give EU investors only limited access to its market. Beijing will stop any attempts to compete with its state-supported industries.

DOES THE CAI MAKE INVESTING SAFER?

- The CAI may provide EU investors with greater certainty in the Chinese market, but it does nothing to reduce the risk of certain investments *from* China.
- As investment from China rises, EU members will still have to scrutinize more investments (particularly mergers and acquisitions) for the sake of their national security.
- An EU framework for reviewing foreign investments went into force in October 2020, and while it can help with information sharing among EU member states, it falls short of preventing unwelcome foreign investments into the EU. Despite prodding from Brussels, some members lack sufficient national-level screening mechanisms.

HOW DOES THE CAI AFFECT THE U.S.?

- The U.S. has been spearheading international efforts to shed light on China's belligerence and abusive trade practices on several fronts. The CAI clouds efforts to make common cause with Europe in areas of shared interest.
- The U.S. and the EU just launched a dialogue on China in October 2020, which will focus on a range of issues, including China's economic relationships.
- If the CAI results in significant market access for the EU (beyond the level of the U.S.–China Phase One agreement), it could put American investors in China at a disadvantage and they could lose market share.
- The CAI may encourage other countries to seek greater economic and political gains in Beijing as well.