Statement of
Gordon G. Chang

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Chinese Investment and Influence in Europe

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Chairman Rohrabacher, Ranking Member Meeks, and distinguished Members of the Committee:

It is a privilege for me to appear before you today, and I thank you for this opportunity.

My name is Gordon Guthrie Chang. I am a writer and live in Bedminster, New Jersey.

I worked as a lawyer in Hong Kong from 1981-1991 and in Shanghai from 1996-2001. Between these two periods, I frequently traveled to Asia from California. I regularly go to Asia now.

I am the author of *The Coming Collapse of China* (Random House, 2001) and *Nuclear Showdown: North Korea Takes On the World* (Random House, 2006).

I am a Daily Beast columnist and write for other publications from time to time. I concentrate on Asia, especially China and North Korea.

Conclusion

This testimony looks at how China views Europe, other than Russia, in the context of Beijing's attempts to dominate technology sectors.

I conclude that Europe is where China is trying to undermine the United States, especially subverting American curbs on acquisition of sensitive technologies.

Chinese Ambitions

Whether China is a "revisionist" or "revolutionary"[1] power, it will need to dominate technology if it is to realize its broad—and fast expanding—ambitions.

Xi Jinping, the Chinese ruler, has put technological dominance close to the top of his agenda. There is, most infamously, his Made in China 2025 initiative, which seeks self-sufficiency in ten sectors, such as aircraft, robotics, electric cars, and computer chips. An "updated national plan," released January of this year, emphasizes 5G, the next generation of wireless communications.

CM2025, as the initiative is known in China, is at the heart of Xi's industrial policy, and his industrial policy is at the heart of his plan to make China the world's technological leader and dominant economy. To achieve the goals of the plan, Beijing offers large low-interest loans from state investment funds and development banks; generous research subsidies; and, most relevant to this testimony, assistance for acquisitions of foreign technology.

This government support for acquisitions is certainly the best explanation of why Midea Group, a Chinese manufacturer of home appliances like air conditioners and microwave ovens, would purchase Kuka AG, known as Germany's foremost robotics company.

Companies diversify of course, but the takeover of a foreign concern that far afield from the acquirer's core business looks government-directed or at least motivated by government wishes, especially because the acquisition netted China a technology that had been targeted by Beijing's most important industrial policy.

In this case, a Chinese company had spare cash and Chinese technocrats saw an opportunity to act. In the absence of government support or involvement, it is extremely unlikely Midea would have even thought of going to the other end of the Eurasian landmass to buy a business so unrelated to its own.

CM2025's support for acquisitions of technology supplements Beijing's "Go Out" or "Go Global" strategy, an effort, dating to 1999, to encourage Chinese enterprises to acquire foreign businesses.

Takeovers of such businesses declined last year—outbound non-financial investment fell 29.4% according to China's Commerce Ministry.[2] Does this mean Beijing's support for foreign acquisitions is on the wane?

No. Chinese officials, worried about accelerating capital flight evident in 2015 and 2016, clamped down hard on acquisitions. The crackdown on capital movements, however, does not seem to have crimped the central government's effort to buy foreign technology.

Beijing's preferred target has been, of course, the United States of America. There, China has been shrewd in buying or funding start-ups and scooping up distressed U.S. tech companies.

In short, whether in Europe or the United States, much of the China's outbound investment in the past half-decade is in areas targeted by either Made in China 2025 or Beijing's 12th and 13th Five-Year Plans, which together cover the decade ending 2020.

American Response

China's ambitions, backed by its state-directed campaign, worry American policymakers. Zheng Yongnian of the National University of Singapore maintains the West is on "high alert" on China, believing, in the words of the *South China Morning Post*, that "the U.S. was launching a technology cold war against the country."[3]

"Cold war" is an overstatement. Although there have been some U.S. prohibitions on Chinese tech acquisitions, China has mostly been able to buy what it wants. American officials, for instance, did not block Midea's suspicious purchase of Kuka, as they had the power to do.[4]

Nonetheless, it is true Chinese tech acquisitions in the U.S. have become harder as a practical matter in the last couple years. In high-profile cases, U.S. authorities have sometimes stopped Chinese money from scooping up American technology.

Presidents Obama and Trump, for example, used their power to derail large deals. In December 2016, Obama by executive order implemented the recommendation of the Committee on Foreign Investment in the United States and blocked a $723 million Chinese bid to purchase Aixtron, a German-based concern making equipment used in fabricating semiconductors. The prohibition was only the third time an American president had implemented a recommendation from CFIUS, as the interagency committee is commonly called, to stop a transaction.

The fourth and fifth times came in the Trump administration. Trump in September of his first year in office prevented Canyon Bridge Capital Partners, a Chinese-controlled buyout fund, from taking over chipmaker Lattice Semiconductor Corp. Then in March of this year the president ordered Broadcom, then a Singapore-incorporated company, to drop efforts to buy Qualcomm, the San Diego-based chipmaker.

The later action was especially noteworthy because, although none of the parties were Chinese, Trump had China in mind while ordering the prohibition. A Broadcom victory in a hostile contest was considered to also be a victory for China. Why? If successful, the Singapore company, in an effort to lift shareholder value, would almost certainly have sold off Qualcomm assets quickly, reduced R&D budgets substantially, and controlled costs ruthlessly. That would have pleased markets but made it difficult, as a practical matter, for the U.S. to compete in the global race for 5G.[5]

With Qualcomm out of the 5G race, China's Huawei Technologies, which receives substantial backing from Beijing, would have been able to set global standards and end up the world's 5G provider. As the Broadcom-Qualcomm battle shows, these days any transaction having China implications is going to get a thorough CFIUS review. Bloomberg reports that CFIUS concerns have led to the abandonment of several technology deals as the Trump administration moves with determination to protect American innovation.[6]

As it should. There is pending legislation, sponsored by Senator John Cornyn, the Texas Republican, to expand CFIUS's authority. "CFIUS needs to get much smarter and more agile," Alan Tonelson told Fox News in early March. "Regimes like China's nowadays can access knowhow through multiple channels both direct and indirect. CFIUS's mandate needs to be flexible enough to cover all those currently existing and new schemes as they emerge."[7]

Due to its recent activity, CFIUS has become one of Beijing's targets recently. The *Washington Post* reported this month that Beijing had handed U.S. trade negotiators a list of its "economic and trade demands."[8] Many of those demands, when read together, told the Trump administration it had to drop restrictions on acquisition of U.S. technology. "They expect to be treated the same way our treaty allies are treated, which is ridiculous," Derek Scissors of the American Enterprise Institute told the paper, speaking of the Chinese.

In the atmosphere in Washington these days, that demand, in Scissors's words, is "crazy," and the Chinese know it, which is why they have instead been trying to buy European tech, in many cases comparable to America's. The stakes for the United States are enormous because the success of its export-control regime depends on getting European capitals to control tech transfers, by acquisition or otherwise.

The risk is not theoretical, unfortunately, and Shenzhen-based Huawei, the world's leading telecom-equipment maker, is a case in point. The company, thought to have close linkages with China's People's Liberation Army and the Chinese security services, is being shut out of the U.S. market due to national security concerns.

Yet Huawei has been able to bypass America. The fast-growing Chinese company "has invested billions across the Continent" and now derives a stunning 35% of its revenues from Europe.[9] Huawei, in comparison to its fortunes in the United States, "has had better luck in Europe."[10] And Huawei is not the only Chinese company to adopt a shun-U.S.-embrace-Europe strategy.[11]

European Response

Of course, China is getting European tech in many ways, one being through European investment into China. In China, of course, intellectual property is either stolen or lost through leaching.

In this regard, on May 18 Xinhua News Agency announced that two entities in Chengdu, the Chengdu High-Tech Industrial Development Zone and China Taiping Investment Holdings, established a fund of 1 billion yuan ($157 million) for the purpose of "technology transfer and achievement transformation between China and the EU." The choice of the city is significant because Chengdu is making itself into a technology center for Europe. It is, for instance, the site of the EU-China Business and Technology Cooperation Fair, which has already had 12 sessions.[12]

European companies, like their American counterparts, are wary of transferring their best tech to China, so the greater concern for the U.S. is Chinese acquisition of Europe's best tech by buying European companies. The Chinese are acquiring a lot, and the pace is accelerating fast.

According to Bloomberg News's most recent calculations, Chinese parties have purchased or invested at least $318 billion in Europe during the last 10 years. China has poured 45% more into Europe than in the U.S. during the period. China, the news organization notes, has acquired 360 European companies since 2008.[13]

Chinese investment, despite the recent downturn caused by tightened capital controls, is on a general upswing. As Bloomberg reports, "2016 was by far the biggest year for Chinese dealmaking in Europe."[14]

Another source highlights the big increase in China's commitment to the Continent: Chinese foreign direct investment into Europe in 2010 was 1.6 billion euros, rising to 35 billion euros in 2016.[15]

The mix of Chinese investments is also changing. Investment in tech, undoubtedly due to Beijing's direction, is on the rise. "In the early years, Chinese investors took advantage of the benefits the less-developed southern European economies could provide and invested in a wide range of sectors, from real estate to entertainment," writes Magda Tsakalidou, an analyst studying Chinese investment patterns in Europe. "Now, their investment policy has become more strategically planned, aiming at long-term national benefits. Chinese investors are redirecting their efforts to the three major European economies—Germany, the U.K., and France—and targeting manufacturing enterprises and high-tech firms."[16] Some add Italy to that group.[17]

As Tsakalidou notes, China's relatively recent move to buy European tech has concerned the Continent's leaders.[18]

The latest U.S. National Security Strategy, issued by the Trump administration in December, states "China is gaining a strategic foothold in Europe" by, among other tactics, "investing in key industries, sensitive technologies, and infrastructure."[19]

That strategic foothold should not be a surprise. Europe does not have a tech-control regime.

Europe, however, is struggling to develop one. An EU Commission paper, issued May 2017, stated "concerns have recently been voiced about foreign investors, notably state-owned enterprises, taking over European companies with key technologies for strategic reasons."[20] Little, however, has been done to address those concerns, even after Midea's early 2017 purchase of Kuka.[21]

Germany, the home of Kuka, along with France and Italy wanted EU leaders at a June 2017 EU Council summit to call on the EU Commission to consider "ways to screen investments from third countries." Although the three countries managed to get their language into draft statements, the final version of the summit document did not include their proposal. Smaller states, which had benefitted from Chinese investment, blocked the initiative.[22]

A draft EU Commission regulation, released in September of last year, would permit the Commission to screen for "security and public order" that was "likely to affect projects or programs of EU interest." The regulation, however, would not give the Commission the power to block an investment.[23]

At the moment, only 12 of the 28 EU member states have screening rules.[24]

Incidentally, Europe is the number one destination for Chinese investment in part because it does not have a mechanism in place to stop foreign investment.[25] So Europe is the gaping hole in American efforts to stop the flow of tech to China.

The EU, with so many member states and its unanimity rule, is particularly susceptible to Beijing's divide-and-conquer strategy. China, by dividing and conquering, has been able to get what it wants, at least most of the time.

There are reasons for hope, however. First, the two core members of the EU are especially concerned about protecting European innovation from Chinese acquisition. French President Emmanuel Macron publicly advanced the notion of a "protective Europe"[26] in the context of the security threatened by China's investments. He did not get his way in EU councils, as evident from recent events, but he has not given up.

Moreover, Macron has an important ally, German Chancellor Angela Merkel. Her vice chancellor, Sigmar Gabriel raised the reciprocity point that has gained traction in the

United States, recently stating his country should not sacrifice "its companies on the altar of free markets" while Beijing shuts German companies out of the Chinese market.[27]

So while Beijing has been looking for and found its "points of entrée" in the eastern and southeastern EU member states, the heart of the organization—where much of the valuable technology is found—is putting up a stout defense.

And that defense is urgently needed. As Bloomberg notes about Chinese investment, "More than half of the known investment total is concentrated in Europe's five largest economies."[28]

Second, what European countries will not protect, the United States will. As mentioned above, the Obama administration blocked China's bid for Aixtron. Specifically, the U.S. in December 2016 refused to permit the transfer of a U.S.-incorporated subsidiary to a German sub controlled by China's Fujian Grand Chip Investment Fund. Prior to Obama's action, Berlin withdrew approval for the acquisition, but only after Washington had urged it to do so.[29]

So American administrations can, as a practical matter, prevent Chinese takeovers of some European tech-heavy companies, and in other cases the U.S. can stop or at least control such acquisitions through export-controls on licenses of American tech.

American Political Will

"We will work with our partners to contest China's unfair trade and economic practices and restrict its acquisition of sensitive technologies," the 2017 National Security Strategy states.[30]

Working with partners, European and otherwise, has not always been easy when the issue is China. As an initial matter, the issue is not whether America has the leverage over Europe to stop Chinese acquisitions of European technology. The issue is whether Washington has the political will to use that power. Political will, to a great extent, is the result of perceptions of the harm China can do with its possession of technology. Many, unfortunately, see China as benign.

China is not. By now, political leaders on both sides of the Atlantic should realize that Beijing is absolutely determined to control technology and will stop at little to obtain it. And it is up to the United States to figure out strategies, both hard and soft, to get Europe to plug the hole through which tech is pouring out of the West into the hands of a rapacious China.

[1] Xi Jinping looks like he wants to replace the current international system with a China-centric order. *See* Gordon G. Chang, "Trump's 'Beautiful Vision' vs. China's Imperial Dream," National Interest, December 27, 2017, http://nationalinterest.org/feature/trumps-%E2%80%98beautiful-vision%E2%80%99-vs-chinas-imperial-dream-23826.

[2] "China's Outbound Investment Slumped in 2017 as Deals Scrutinized," Bloomberg News, January 16, 2018, https://www.bloomberg.com/news/articles/2018-01-16/china-s-outbound-investment-slumped-in-2017-as-deals-scrutinized.

[3] Wendy Wu and Robert Delaney, " 'It's Not Over Yet': Key Sticking Points Remain for US and China on Trade, Analysts Say," *South China Morning Post* (Hong Kong), May 21, 2018, http://www.scmp.com/news/china/diplomacy-defence/article/2146983/its-not-over-yet-key-sticking-points-remain-us-and?from=groupmessage&isappinstalled=0. China's moving up the tech scale has alarmed American and European officials. *See*, *e.g*., Thomas L. Friedman, "The U.S. and China Are Finally Having It Out," *New York Times*, May 1, 2018, https://www.nytimes.com/2018/05/01/opinion/america-china-trump-trade.html.

[4] *See* "China's Midea Receives U.S. Green Light for Kuka Takeover," Reuters, December 30, 2016, https://www.reuters.com/article/us-kuka-m-a-mideamidea-group-idUSKBN14J0SP.

[5] *See* Gordon G. Chang, "Why the Bid to Buy Qualcomm Poses a Dire Threat to US National Security," Fox News Opinion, March 2, 2018, http://www.foxnews.com/opinion/2018/03/02/why-bid-to-buy-qualcomm-poses-dire-threat-to-us-national-security.html.

[6] *See* David McLaughlin, "Trump Blocks Broadcom Takeover of Qualcomm on Security Risks," Bloomberg Politics, March 12, 2018, https://www.bloomberg.com/news/articles/2018-03-12/trump-issues-order-to-block-broadcom-s-takeover-of-qualcomm-jeoszwnt.

[7] Chang, "Why the Bid to Buy Qualcomm Poses a Dire Threat to US National Security."

[8] Josh Rogin, "China Gave Trump a List of Crazy Demands, and He Caved to One of Them," *Washington Post*, May 15, 2018, https://www.washingtonpost.com/news/josh-rogin/wp/2018/05/15/china-gave-trump-a-list-of-crazy-demands-and-he-caved-to-one-of-them/?utm_term=.45bb5b2c98d9.

[9] Laurens Cerulus, "Europe Turns Cool on Chinese Tech," Politico Europe, May 9, 2018, https://www.politico.eu/article/europe-reaches-moment-of-reckoning-over-5g-security-huawei-us-donald-trump-cybersecurity/.

[10] Yukon Huang, "Why China Invests More in Europe Than in the US," *Financial*

Times (London), July 24, 2017, https://www.ft.com/content/a7641d16-6c66-11e7-b9c7-15af748b60d0.

[11] *See*, *e.g.*, Daniel Ren, "Chinese State Investment Firm to Avoid US and Look to Europe in Pursuit of Tech Assets as Trade Row Deepens," *South China Morning Post* (Hong Kong), April 5, 2018 (China Jianyin Investment, an equity investment vehicle), http://www.scmp.com/business/companies/article/2140369/chinese-state-investment-firm-avoid-us-trade-row-deepens-and-look.

[12] "First EU-China Tech Scale-Up Summit Yields Fruit," Xinhua News Agency, May 18, 2018, http://www.xinhuanet.com/english/2018-05/18/c_137189707.htm.

[13] Andre Tartar, Mira Rojanasakul, and Jeremy Scott Diamond, "How China Is Buying Its Way into Europe," Bloomberg News, April 23, 2018, https://www.bloomberg.com/graphics/2018-china-business-in-europe/.

[14] Ibid.

[15] *See* Friso Stevens, "Europe Ponders How to Curb China's High-Tech Buying Spree," Diplomat, February 16, 2018, https://thediplomat.com/2018/02/europe-ponders-how-to-curb-chinas-high-tech-buying-spree/.

[16] Magda Tsakalidou, "Has Winter Come for Chinese Investments in the EU?" Diplomat, October 24, 2017, https://thediplomat.com/2017/10/has-winter-come-for-chinese-investments-in-the-eu/.

[17] *See*, *e.g.*, Stevens, "Europe Ponders How to Curb China's High-Tech Buying Spree."

[18] Tsakalidou, "Has Winter Come for Chinese Investments in the EU?"

[19] "National Security Strategy of the United States of America," December 2017, https://www.whitehouse.gov/wp-content/uploads/2017/12/NSS-Final-12-18-2017-0905.pdf.

[20] EU Commission, "Reflection Paper on Harnessing Globalisation," May 10, 2017, https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-globalisation_en.pdf.

[21] Midea's purchase triggered concerns among European policymakers and leaders. *See*, *e.g.*, Tsakalidou, "Has Winter Come for Chinese Investments in the EU?"

[22] Congressional Research Service, memorandum to House Subcommittee on Europe, Eurasia, and Emerging Threats, May 15, 2018.

[23] Ibid.

[24] Stevens, “Europe Ponders How to Curb China’s High-Tech Buying Spree.”

[25] Tartar, Rojanasakul, and Diamond, “How China Is Buying Its Way into Europe.”

[26] Arthur Beesley, “Macron and Allies Head for EU Clash on Foreign Takeovers,” *Financial Times* (London), June 15, 2017, https://www.ft.com/content/73aadc3a-5118-11e7-bfb8-997009366969.

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[29] *See* Maria Sheahan, “China’s Fujian Drops Axitron Bid After Obama Blocks Deal,” Reuters, December 8, 2016, https://www.reuters.com/article/us-aixtron-m-a-fujian/chinas-fujian-drops-aixtron-bid-after-obama-blocks-deal-idUSKBN13X16H.

[30] National Security Strategy of the United States of America.