EU Toolkit for Economic Security and De-risking

As the dynamics of international politics and global trade continue to evolve, the EU has developed a toolkit seeking to safeguard its economic interests. The list of tools generated by the bloc is wide and increasing, ranging from the Foreign Subsidies Regulation and the Carbon Border Adjustment Mechanism to initiatives like the Net-Zero Industry and Cybersecurity Acts.

In this review, we start with seven relevant trade policies (listed in the order of the time of original initiation) adopted by the EU, exploring their purpose, status, and potential implications for EU-China relations. As these mechanisms can play a crucial role in shaping trade dynamics, understanding their impact is essential for stakeholders on both sides.

As a disclaimer, this is a non-exhaustive list, and it is likely to undergo some future modifications, additions and updates following further developments.

1. Outbound Investment Mechanism
2. Carbon Border Adjustment Mechanism (CBAM)
3. Anti-Coercion Instrument (ACI)
4. Critical Raw Materials Act (CRMA)
5. Foreign Subsidy Regulation (FSR)
6. Framework for Screening Foreign Direct Investments (FDI)
7. International Procurement Instrument (IPI)

RELEVANT CONCEPTS

The following section gathers the definitions of relevant concepts pertinent to the topic in an effort to provide an understanding of the political context fostering the proposal of some of the tools listed above.

- ***DE-RISKING***

Von der Leyen introduced the term, as an alternative to the concept of decoupling, at a speech delivered on 30 March 2023 when addressing the relationship between China and the EU. Both in diplomatic and economic terms, de-risking links to the EU's consciousness of its dependencies and emerges response trying to re-balance its economic relationship with one of its largest trading partners (including China). The initial proposal based de-risking on two pillars: economic and diplomatic (*see Speech by President von der Leyen on EU-China relations to MERICS and the EPC*). Providing further insights on the EU-China Summit held in December 7-8, 2023, on the HRVP's blog, Borrell mentioned the clarification efforts on explaining the EU's stance on de-risking, stating that the strategy is "not an anti-Chinese move, but a matter of common sense and of risk management." The Representative also highlighted that "it is not the EU's goal to decouple from China, but we must safeguard our economic security by addressing excessive dependencies and diversifying our supply chains" (*see EU-China Summit - Of Rivalry and Partnership*). Overall, de-risking might still be a complex and evolving concept, as its implementation is currently unfolding, thus yet to be fully clarified and even open to debates.

- ***ECONOMIC SECURITY***

The term does not retain a fully-fledged definition, probably due to its complexity and broadness. However, under the umbrella of the Economic Security Strategy launched by the European Commission and HRVP Josep Borrell, the concept was used to refer to the overall objective of protecting "EU interests against the weaponisation of economic ties". Borrell's blog states that, in essence, "economic security is about using economic measures and tools for security purposes" to address a set of risks that "can challenge the functioning of our democratic societies and of our economies by limiting our ability to act" (*see EEAS Website*).

Ursula Von der Leyen's presentation of said strategy adds more comprehensiveness to the term, stating that the concept builds on "three policy strands": 1) promoting competitiveness in Europe; 2) protecting Europe from the risks identified; and 3) partnering with others to bolster research cooperation and strengthen trade relations and supply chains (*see Statement by the President on today's College meeting*).

- ***STRATEGIC AUTONOMY***

The European Parliamentary Research Service defines the concept as "the capacity of the EU to act autonomously – that is, without being dependent on other countries – in strategically important policy areas". Concerning the stated policy areas, these can fluctuate from "defence policy to the economy, and the capacity to uphold democratic values" (*see EU Strategic Autonomy Monitor*).

In the HRVP's blog, Josep Borrell published a post explaining the concept, in which he wrote that the former did not constitute a new addition to the EU vocabulary. The Representative stressed that given its birth in the field of defence industry, the defence and security dimension of the term remains predominant and sensitive. However, the stakes of strategic autonomy go beyond, thus applying to a wide range of issues including trade, finance and investments (*see Why European strategic autonomy matters*).

- ***OPEN STRATEGIC AUTONOMY***

The European Parliamentary Research Service EU Strategic Autonomy Monitor indicates that the term shares similitudes with the one of strategic autonomy. However, the addition of "open" appeared to alleviate the reservations of some Member States preventing an increase in the EU's capacity to act, and the fears that strategic autonomy will hamper free trade and free competition (*see EU Strategic Autonomy Monitor*).

A policy report written by the Joint Research Centre states that the term presents several core features, including "notions of a future state of enhanced resilience, managed mutual interdependence and relative power evolving from existing capacities, vulnerabilities, and dependencies". Moreover, the term is about cutting across multiple policy areas (*see JRC Shaping and Securing the EU's Open Strategic Autonomy by 2040 and Beyond*).

1. OUTBOUND INVESTMENT MECHANISM

Background

In the context of post-pandemic, Russia's war in Ukraine, hostile economic actions and a global increase in geopolitical tensions, the EU identified a risk linked to outbound investment, particularly on its dual use in a narrow set of advanced technologies that could potentially threaten both EU's economic security as well as international peace and security. In front of this scenario, in the "European Economic Security Strategy" presented on 20 June 2023, the Commission expressed its intention to propose an initiative by the end of the year on a measure addressing the risks related to outbound investments.

Purpose and Objective as stated by the EU

To prevent the narrow set of technological advances assessed to be core to enhancing military and intelligence capabilities of actors who may use them to undermine international peace and security from being fuelled by our companies' capital, expertise and knowledge. Moreover, to bolster economic resilience and protect essential security interests, bearing in mind also the impacts outside the EU.

Key Terms (based on the definitions provided by the EU):

- **Dual-use products:** "goods designed for civilian use that in the wrong hands could be used to suppress human rights or launch terrorist attacks". Said products can range from "drones to chemicals". *See European Parliament News.*

Timeline:

- **20 June 2023** → The Commission presents a joint communication together with the High Representative for Foreign Affairs and Security Policy on a European Economic Security Strategy, establishing the Commission's intention to proposing an initiative by the end of the year on a measure addressing the risks related to outbound investments.

Debates & Discussions

In addition to the difficulties inherently linked to the control of outbound investment, the European Commission is faced with the additional complication of a divergence in opinion on whose competence this aspect of FDI is. What leaves, consequently, an open door to multiple unanswered questions.

Materials addressing what it entails for EU-China relations

- Herbert Smith Freehils - EU moves towards outbound investment controls: a geopolitical European Commission shifts gear
- Trade Practitioner for Foreign Investment Reviews - "REVERSE FDI" Towards an EU Outbound Investment Control Regime?

Exemplary cases

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2. CARBON BORDER ADJUSTMENT MECHANISM (CBAM)

Background

To accompolish the European Green Deal (2019), and as part of the 'Fit for 55' package (an initiative to reduce the EU's greenhouse gas (GHG) emissions by 55 percent by 2030), the CBAM was designed to contribute and facilitate the EU's goal of reaching climate neutrality by 2050. With this goal in mind, the EU found key to avoid EU-based companies to relocate their carbon-intensive production to countries counting with less strict climate policies, as well as for EU products to get replaced by more carbon-intensive imports.

Purpose and Objective as stated by the EU

To put a fair price on the carbon emitted during the production of carbon-intensive goods entering the EU. The idea is to encourage cleaner industrial production in non-EU countries while countering the 'carbon leakage' risk by establishing an import tariff on carbon-intensive goods from all countries abroad and not belonging to the EU ETS.

The CBAM is initially covering seven industrial sectors (iron and steel, cement, fertilisers, aluminium, electricity generation, and hydrogen) selected after their risk of carbon leakage, the magnitude of their carbon emissions, and for administrative feasibility.

Key Terms (based on the definitions provided by the EU):

- **Carbon leakage:** "The situation that may occur if, for reasons of costs related to climate policies, businesses were to transfer production to other countries with laxer emission constraints. This could lead to an increase in their total emissions." *See Carbon Leakage*.

Timeline

- **14 July 2021** → The Commission presents a draft proposal for a Regulation of the European Parliament and the Council establishing a carbon border adjustment mechanism.
- **13 December 2022** → A provisional agreement on the CBAM is reached.
- **10 May 2023** → Regulation (EU) 2023/956 of the European Parliament and of the Council of establishing a carbon border adjustment mechanism is adopted, entering into force one day after its publication in the Official Journal of the European Union on **May 16, 2023**.
- **1 October 2023** → The CBAM enters into application in its transitional phase, with the first reporting period for importers ending on **31 January 2024** and culminating in **December 2025**.

Next steps:

- **1 January 2026** → The permanent system will enter into force, requiring importers to declare each year the quantity of goods imported into the EU in the preceding year and their embedded GHG.

Debates & Discussions

Developing countries have shared their concerns on the CBAM's potential to turn into a trade barrier if used as a discriminative tool impacting the competitiveness of external exports. Moreover, the mechanism is expected to impact this set of countries by reducing the trade levels, and producing losses in GDP, leaving low- and middle-income countries' voices appear not being heard on several issues.

Materials addressing what it entails for EU-China relations

- Christopher Kardish, Lina Li, and Mary Hellmich (Adelphi) & Maosheng Duan and Yujie Tao (Tsinghua University) for Adelphi - The EU carbon border adjustment mechanism (CBAM) and China Unpacking options on policy design, potential responses, and possible impacts.
- Deloitte's Sustainability Spotlight Series No.50 - CBAM and its implications for companies in China
- Olivia Rumble and Andrew Gilder for African Climate Wire - WTO Review of EU Trade Policies highlights significant unease about CBAM
- Hanh Duong, Fan Yang, Yidi Zeng, Jingyi Zhu, and Kun Li for The SAIS Review of International Affairs - Unveiling Carbon Border Adjustment Mechanism (CBAM) Challenges: The Potential Dispute Between China and EU
- Jianwu He, and Shantong Li for the GTAP Annual Conference on Global Economic Analysis - The impact of EU's Carbon Border Adjustment Mechanism on China's economy
- Joe Cash for Reuters - China urges EU to ensure new carbon tax complies with WTO rules

Exemplary cases

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3. ANTI-COERCION INSTRUMENT (ACI)

Background

The policy response was initially stirred by concerns linked to the Trump administration. However, after a year of multiple confrontations between the EU and Beijing, marked by the country's alleged unofficial trade embargo against Lithuania due to its alleged breach of EU's 'One-China Policy', the instrument eventually developed around worries over China's leverage of economic linkages. Moreover, recognizing economic coercion as a risk, the instrument has become a central element in the bloc's economic security strategy presented in June 2023.

Purpose and Objective as stated by the EU

To deter any potential economic coercion and provide a structure to get the third country to stop the coercive measures through dialogue and engagement if such coercion ends up taking place. In case of failed engagement, the tool gives the EU access to a wide range of possible countermeasures against the coercing country (including the imposition of tariffs, restrictions on trade in services, and restrictions on access to foreign direct investment or public procurement).

Key Terms (based on the definitions provided by the EU):

- **Economic Coercion:** "A situation where a third country attempts to pressure the EU or a Member State into making a particular choice by applying, or threatening to apply, measures affecting trade or investment against the EU or a Member State." *See the Commission's press release Political agreement on new Anti-Coercion Instrument to better defend EU interests on the global stage.*

Timeline

- **8 December 2021** → The Commission presents a proposal for a Regulation of the European Parliament and of the Council on the protection of the Union and its Member States from economic coercion by third countries.
- **6 June 2023** → The European Parliament and the Council reach a political agreement including a legal framework, decision-making arrangements and timeframes for EU action.
- **3 October 2023** → The European Parliament approves the new Regulation, which is adopted on October 23 by the Council.

Debates & Discussions

The central debates around the instrument lay on its compatibility with the WTO's rules, with some contesting its motivation and legality, and others defending its relevance in a changing economic order.

Materials addressing what it entails for EU-China relations

- Henry Gao for CIGI - Will the European Union's New Anti-Coercion Instrument Work with China?
- Alice Politi for RSAA – The Paradigm-shift in EU-China Relations and the Limits of the EU's Current Strategy Towards China: A Relational Perspective
- Jonathan Hackenbroich with Filip Medunic and Pawel Zerka for ECFR - Tough trade: The hidden costs of economic coercion

Exemplary cases

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4. CRITICAL RAW MATERIALS ACT (CRMA)

Background

Critical Raw Materials (CRMs) are crucial in a wide range of industrial ecosystems and constitute a central piece in securing Europe's green and digital transitions, leaving the EU relying on the main processors and providers of such minerals and strengthening the bloc's reliance and dependency on them. Hence, learning from the reliance on Russian gas experience before and after its war in Ukraine, witnessing an increase in tensions with China, and with the idea of becoming the first climate-neutral continent, the EU started its path towards the transition.

Purpose and Objective

To ensure a secure and sustainable supply of critical raw materials for Europe's industry and significantly lower the EU's dependency on imports from single-country suppliers. Thus, the Act aims to strengthen the EU's critical raw material capacities along all stages of the value chain and to increase the bloc's resilience by reducing dependencies, increasing preparedness, and promoting supply chain sustainability and circularity. To achieve the former, the CRM Act sets out four specific objectives:

- Strengthening the EU's capacities along the different stages of the value chain (to be ensured by 2030 ideally).
- Diversifying the EU's imports of raw materials to ensure that no third country provides more than 65% of the EU's annual consumption (for each strategic raw material).
- Improving monitoring and risk mitigation.
- Ensuring a well-functioning single market while improving the sustainability and circularity of CRMs.

Key Terms (based on the definitions provided by the EU):

- **Critical Raw Materials:** "Strategically important" materials for the EU's industry and economy and that have "high risks associated with securing their supply". *See the European Parliament Briefing 'Critical raw materials for the EU'*.
- **Circularity:** Referring to the concept of circular economy, a "model of production and consumption, which involves sharing, leasing, reusing, repairing, refurbishing and recycling existing materials and products as long as possible", applied to critical raw materials, the former "mitigates the risks associated with supply, such as price volatility, availability and import dependency." *See Circular economy: definition, importance and benefits*.

Timeline

- **18 May 2020** → A legislative proposal on the supply of CRMs is announced in the REPowerEU Plan presented by the Commission.
- **3 September 2020** → The Commission publishes a Communication to the European Parliament, the Council, the European Economic and Social Committee, and the Committee of the Regions on Critical Raw Materials Resilience: Charting a Path towards greater Security and Sustainability. In the Communication, the European Raw Materials Alliance is announced.
- **November 2021** → The Parliament adopts a resolution on a European strategy for CRMs.

- **30 September 2022** → The Commission launches a call for evidence concerning the future of CRMs act, explaining the package of regulatory and non-regulatory actions the Commission was planning to put forward.
- **1 February 2023** → The Commission publishes the Green Deal Industrial Plan for the Net-Zero Age, in which CRMs are also part of Pillar 1.
- **16 March 2023** → The Commission presents a proposal for a regulation of the European Parliament and of the Council establishing a framework for ensuring a secure and sustainable supply of CRMs and amending Regulations EU) 168/2013, (EU) 2018/858, 2018/1724 and (EU) 2019/102071.
- **13 November 2023** → After two rounds of trilogue discussions the Council and Parliament find an agreement during the third one.

Next steps:

- The agreement reached by the Council and the Parliament needs to be approved by Parliament and Council to become law.

Debates & Discussions

Experts have highlighted the need for the EU's partnerships seeking to reduce dependencies to prioritise environmental protection, human rights, and the well-being of communities in third countries to enhance the importance of the global justice approach. Yet, it has been argued the bloc's intention to reach such autonomy can imply multiple hurdles like social unrest and potential conflict risks if not done properly. In this regard, the strategy needs to remain international and avoid relying exclusively on domestic measures.

Materials addressing what it entails for EU-China relations

- Geological Survey of Sweden - Critical and strategic raw materials
- EUR-Lex - 52023PC0160 - Proposal for a Regulation of the European Parliament and of the Council establishing a framework for ensuring a secure and sustainable supply of critical raw materials and amending Regulations (EU) 168/2013, (EU) 2018/858, 2018/1724 and (EU) 2019/1020
- Andy Home for Reuters - China flexes critical metals muscles with export curbs
- Patrick Schröder, Pepijn Bergsen, and Jack Barrie for Chatham House - Europe's pursuit of securing critical raw materials for the green transition

Exemplary cases

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5. FOREIGN SUBSIDY REGULATION (FSR)

Background

Providing their recipients with an unfair advantage to acquire companies or obtain public procurement to the detriment of fair competition, foreign subsidies have been considered to distort the EU's internal market. In this context, the bloc decided to develop a foreign subsidy regulation that closes, in turn, a regulatory gap.

Purpose and Objective

To address the distortions caused by foreign subsidies allowing the market to remain open to trade and investment while ensuring a level playing field for all companies operating in the Single Market. The regulation applies to all economic activities in the EU, covering concentrations (mergers and acquisitions), public procurement procedures, and all other market situations.

Key Terms (based on the definitions provided by the EU):

- **Distortions:** Deriving from foreign subsidies, these can occur "if an undertaking benefitting from the foreign subsidy engages in an economic activity in the Union". *See Regulation (EU) 2022/2560.*
- **Foreign subsidies:** A "direct or indirect financial contribution by a non-EU country, which is limited to one or more companies or industries and which confers a benefit on a company active in the Single Market. These can come in the form of: interest-free loans, unlimited guarantees, capital injections, preferential tax treatment, tax credits, grants, etc. *See Foreign Subsidies Regulation.*

Timeline

- **21/22 March 2019** → The European Council asks the Commission to identify new tools to address the distortive effects of foreign subsidies on the Single Market.
- **17 June 2020** → The Commission adopts a White Paper on foreign subsidies in the Single Market.
- **5 May 2021** → The Commission presents a proposal for regulation on foreign subsidies distorting the Single Market.
- **30 June 2022** → The European Parliament and the Council agree on the proposal presented by the Commission.
- **12 January 2023** → The Foreign Subsidies Regulation ('FSR'), Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market, enters into force.
- **12 July 2023** → The Commission is able to launch ex-officio investigations.
- **12 October 2023** → The notification obligation for companies becomes effective.

Debates & Discussions

While several actors welcomed the proposal, like BusinessEurope, ETUC, AEGIS Europe..., others, such as the American and Chinese Chambers of Commerce to the EU, cautioned that the proposed mechanisms may unintentionally hamper legitimate investments, or even increase transaction costs and risks and creating uncertainty, respectively.

Materials addressing what it entails for EU-China relations

- Jonathan Branter and Alexander Rose for DWF Group - How will international businesses be affected by the new EU Foreign Subsidies Regulation?
- Laurie Clarke for TechMonitor - The EU’s crackdown on state-subsidised companies is aimed squarely at China
- Rhodium Group and MERICS - EV battery investments cushion drop to decade low: Chinese FDI in Europe 2022 Update
- Global Times - Chinese companies concerned about EU's Foreign Subsidies Regulation
- Priyanka Shankar for SCMP - China firms warn EU foreign subsidy rule could hit investor confidence

Exemplary cases

+ Potentially Chinese investments into wind turbines - See Bloomberg’s article *Europe’s Foreign Subsidy Rules Have China in Its Sights*.

6. FRAMEWORK FOR SCREENING FOREIGN DIRECT INVESTMENTS (FDI)

Background

Given the interconnectedness and integration between the markets of EU Member States, foreign investment could pose a risk for security or public order beyond the state where said investment is made. And in front of the growing concerns regarding certain foreign investors, the lack of a comprehensive framework at the EU level for the screening of FDI investments on the grounds of security or public order, together with the fact that some of the bloc's major trading partners had already developed such frameworks, the EU decided to step up and outline its own FDI screening framework.

Purpose and Objective

To improve the EU's capacity to identify and address potential risks for security or public order in more than one member state deriving from certain transactions while remaining an area open to investments. Moreover, to ensure that the regulation remains updated to the changing security context, the Commission conducts a consultation whose results may lead to a revision of the rules, keeping the focus of the framework exclusively on security and public order.
The regulation does not require member states to set up their own screening at a national level but strongly encourages and recommends doing so.

Key Terms (based on the definitions provided by the EU):

- **Foreign Direct Investment:** "A category of cross-border investment in which an investor resident in one EU country establishes a lasting interest in and significant degree of influence over (ownership of 10% or more of the voting power), a business resident in another country." *See Foreign Direct Investments (FDI).*

Timeline

- **29 November 2017** → The Commission establishes a group of experts from Member States to discuss issues relating to investment screening, share best practices and lessons learned, and exchange views on trends and issues of common concern relating to foreign investments.
- **19 March 2019** → The Regulation (EU) 2019/452 of the European Parliament and of the Council establishing a framework for the screening of foreign direct investments into the Union is adopted, entering into force on **April 10, 2019**.
- **11 October 2020** → The legislation fully applies officially.

Debates & Discussions

A study published by Rhodium Group and MERICS, highlighted the positive outcomes deriving from such framework, as it can provide more certainty on the red lines to be avoided and promote investment in non-sensitive areas. A briefing from the European Parliamentary Research Service, however, highlighted that the mechanism can add to a growing climate of protectionism, likely to impact, beyond its target, the EU itself.

Materials addressing what it entails for EU-China relations

- Rhodium Group and MERICS - EV Battery Investments Cushion Drop to Decade Low. Chinese FDI in Europe 2022 Update
- Gabriele Manca for The Diplomat - Chinese Investment in Europe Is Changing
- Gisela Grieger for the European Parliamentary Research Service - Foreign direct investment screening. A debate in light of China-EU FDI flows
- Paweł Mateusz Gadocha for The Chinese Journal of Global Governance - Assessing the EU Framework Regulation for the Screening of Foreign Direct Investment—What Is the Effect on Chinese Investors?
- Shaohui ZHANG and Yifan ZHANG for Dentons - EU FDI screening and its impact on Chinese investments

Exemplary cases

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7. INTERNATIONAL PROCUREMENT INSTRUMENT (IPI)

Background

Despite the bloc's market openness and accessibility, many of its major trading partners apply restrictive practices in their markets discriminating against EU businesses and affecting competitive sectors. Hence, looking to achieve a certain degree of reciprocal access for the EU's businesses on foreign public procurement markets, the EU designed this instrument. China's increasing industrial weight and its alleged role in backing Russia's invasion of Ukraine further encouraged its adoption in 2022.

Purpose and Objective

To promote reciprocity in access to international public procurement markets while laying down procedures for the European Commission to: 1)investigate alleged measures or practices negatively affecting the access of EU businesses, goods, and services to non-EU procurement markets, and consult with the non-EU countries concerned; and 2) impose, as a last resort, IPI measures to restrict access to EU public procurement procedures for businesses, goods, and services from the non-EU countries concerned.

Key Terms (based on the definitions provided by the EU):

- **Restrictive trade practice:** "Business operation or action that confines or limits the free exchange of goods and services within a country or between countries, which may include discrimination, exclusive dealings, collusion agreements or price fixing." *See European Environmental Agency.*

Timeline

- **21 March 2012** → The European Commission presents a Proposal for a Regulation of the European Parliament and of the Council on the access of third-country goods and services to the Union's internal market in public procurement and procedures supporting negotiations on access of Union goods and services to the public procurement markets of third countries.
- **29 January 2016** → The Commission presents an amended proposal taking on board some recommendations from the Council and the European Parliament, but it does not advance due to differences in Member States' positions.
- **December 2021** → The Parliament adopts its position on the revised IPI proposal, modifying its design, scope and application.
- **9 June 2022** → The Parliament approves the agreement in plenary by a large majority.
- **17 June 2022** → Under Regulation (EU) 2022/1031, the Council formally adopts the instrument, entering into force on **August 29, 2022**.

Debates & Discussions

The IPI received general acceptance from academics and stakeholders. However, throughout the legislative process, the European Economic and Social Committee (EESC) expressed its regret on the insufficient attention given to sustainable development.

Materials addressing what it entails for EU-China relations

- Henry Storey for Hinrich Foundation - “Securing fairness”: Europe unsheathes the International Procurement Instrument
- Rhodium Group and MERICS - EV battery investments cushion drop to decade low: Chinese FDI in Europe 2022 Update
- Simon Lester for China Trade Monitor - The EU's New International Procurement Instrument and Its Impact on China

Exemplary cases

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