CLEARY GOTTLIEB

November 22, 2023

EU FDI: State Of The Union

On October 19, 2023, the European Commission ("**Commission**") published its third annual report on the screening of foreign direct investments ("**FDI**") into the Union (the "**Report**")[1], following previous editions published in September 2022 and November 2021.[2] Notable findings include the following:

— The vast majority of M&A and greenfield FDI into EU have originated from the U.S. and the UK, while FDI from China has steadily declined in the last three years.

— EU FDI lands primarily in Western Europe, and targets 5 main sectors -- Information Communication and Technology, Manufacturing, Professional, Scientific and Technical activities, Finance, and Retail.

— 22 EU Member States now have an active FDI regime, while the remaining 5 EU Member States are expected to join the EU FDI block next year.

— 55% of FDI filings in EU led to screening and decision, up from 29% in 2021 and 20% in 2020.

— 423 FDI filings were reviewed under the EU screening cooperation mechanism,[3] up from 414 in 2021 and 265 in 2020; 90% of the 423 filings originated from only 6 countries – Austria, Denmark, France, Germany, Italy, and Spain.

— The vast majority of notified deals in the EU continue to be cleared unconditionally – 86% in 2022, 73% in 2021, and 79% in 2020. Prohibitions and deal abandonments were limited to 4-5% of the notified deals in 2021 and 2022, a noticeable drop from 9% in 2020, and in line with the Commission's message that the EU is open to FDI and that *"Member States only deny transactions that pose very serious threats to security and public order"*. The remainder (c. 10-20%) of cases required remedies, primarily of a behavioral nature.

— Phase II in-depth reviews focused primarily on the manufacturing and IT sectors. Within manufacturing, FDI agencies targeted energy, cybersecurity, data processing and storage, health, semiconductors, communications, transport, defense, and aerospace.

— Semiconductors remain the most prominent FDI sector likely to attract in-depth scrutiny and potential prohibition (depending on the investor's origin).

---

1 Report from the Commission to the European Parliament and the Council: Third Annual Report on the screening of foreign direct investments into the Union, SWD (2023) 329 final of October 19, 2023.

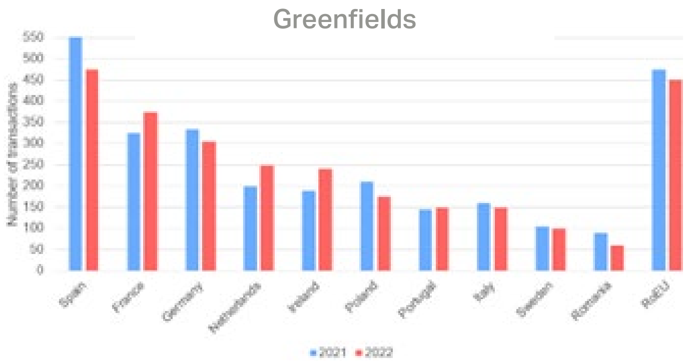
2 Report from the Commission to the European Parliament and the Council: First Annual Report on the screening of foreign direct investments into the Union, SWD (2021) 334 final of November 23, 2021. See also Report from the Commission to the European Parliament and the Council: Second Annual Report on the screening of foreign direct investments into the Union, SWD (2022) 219 final of September 1, 2022.

3 Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union (2019) OJ L791/1.

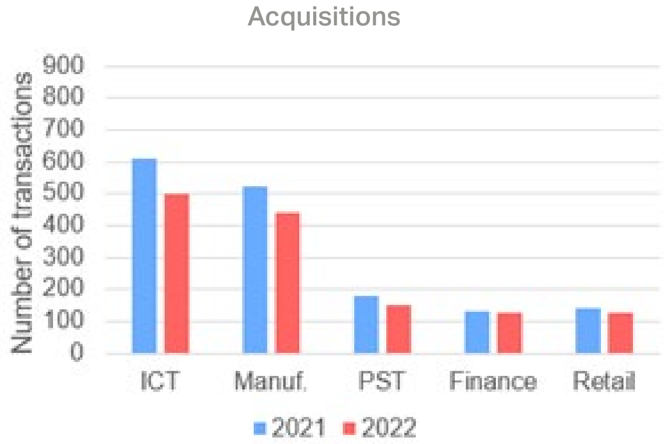
These findings are addressed in more detail below.

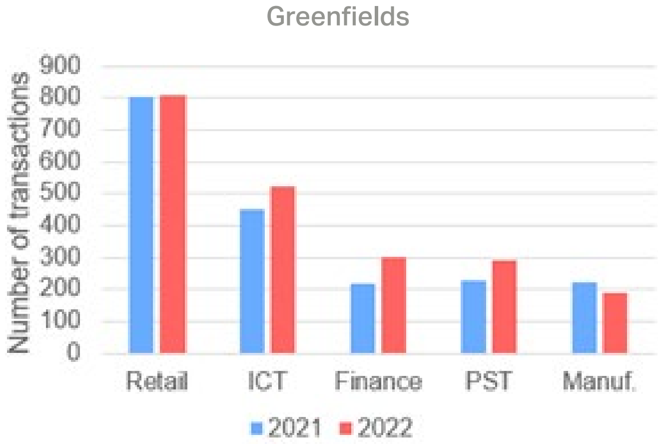
I. EU FDI Overview

Global FDI in 2022 totaled EUR 1.2 trillion, showing a year-on-year decrease of 14.3% compared to 2021. Similarly, number of M&A deals and greenfield investments in Europe declined on a year-on-year basis. EU FDI was attracted primarily from the U.S., which accounted for c. 32% of acquisitions and c. 47% of greenfield investments, and the UK, which accounted for c. 25% of acquisitions and c. 19% of greenfield investments. Conversely, acquisitions and greenfield investments from China have materially declined. FDI acquisitions landed primarily in Germany, Spain, Italy, France, and the Netherlands. FDI greenfield investments were primarily attracted in Spain, France, Germany, the Netherlands, Ireland, and Poland.



FDI acquisitions focused on Information Communication and Technology (**ICT**), Manufacturing, Professional, Scientific and Technical activities (**PST**),[4] Finance, and Retail. Greenfield investments were primarily made in Retail, followed by ICT, Finance, PST, and Manufacturing.





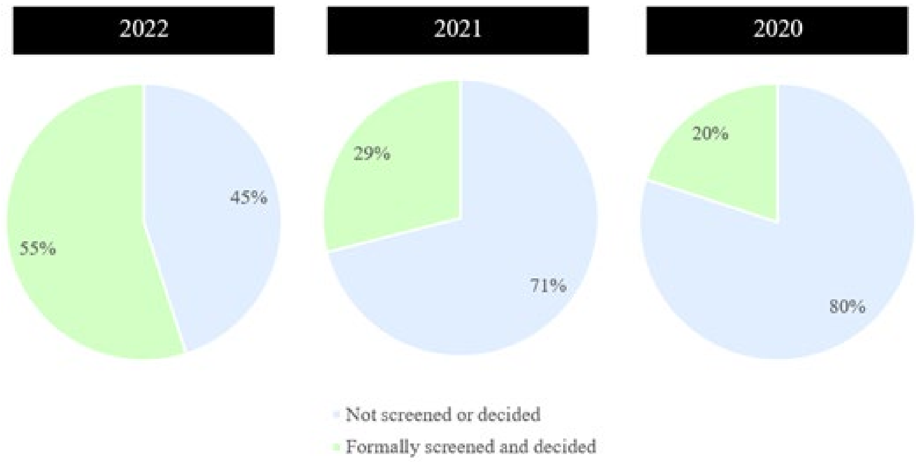
[4] Professional activities include activities by law and accounting firms, as well as consultancy and engineering activities. For example, this encompasses activities of head offices, market research and public opinion polling, consultancy, and research & experimental development on biotechnology. Scientific and technical activities include, among other things, R&D facilities.

II. EU FDI Expansion – Closing The Loop

As anticipated, EU Member States continue to adopt new FDI regimes, in line with the Commission's expectation that all EU Member States *"establish a comprehensive national FDI screening mechanism"*. [5] As of November 2023, 22 EU Member States have an active FDI regime. The remaining 5 EU Member States – Bulgaria, Croatia, Cyprus, Greece, and Ireland – are expected to join the FDI block in the course of 2024.[6]

III. EU FDI Enforcement Trends

While the total number of filings (and *ex officio cases*) decreased, from 1,793 in 2020 and 1,563 in 2021, to 1,444 in 2022, presumably due to drop in deal-making, the level of FDI screening is clearly increasing, with 55% of 2022 filings screened and decided, compared to 29% in 2021 and 20% in 2020. We expect this trend to continue and that the vast majority of FDI filings in coming years will lead to formal screening and decisions.

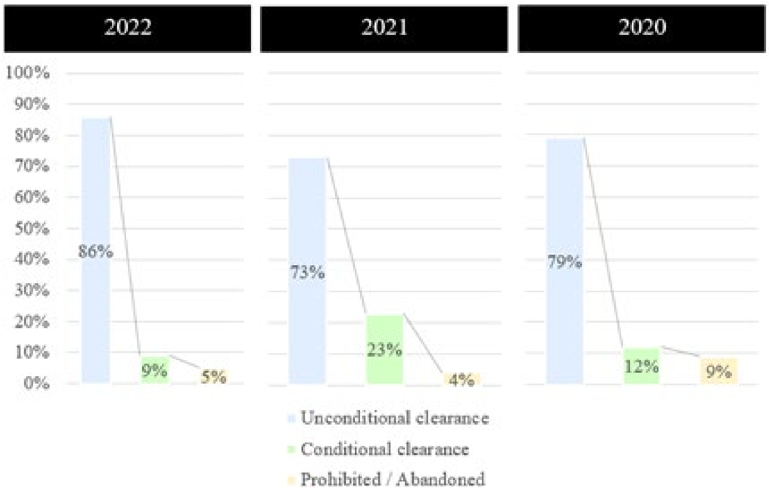


[5] *The Report*, p. 8.

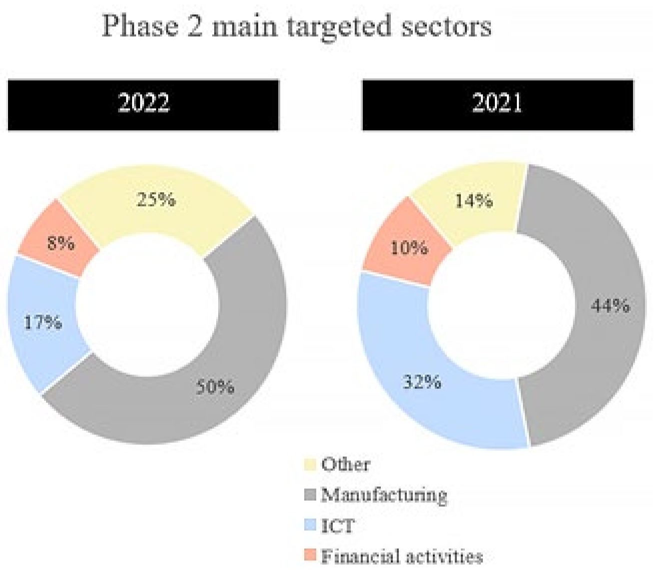
[6] For more granular information on each Member State, please see Commission Staff Working Document: Screening of FDI into the Union and its Member States, COM (2023) 590 final.

Similarly, the number of filings undergoing screening under the EU FDI screening cooperation mechanism[7] continue to increase, from 265 in 2020 and 414 in 2021, to 423 in 2022. Accordingly, 1 out of every 3 FDI filings made at the EU Member State level was shared across the EU for a collective review and comments. The screening mechanism is increasingly utilized across Europe – while 11 EU Member States shared filings in 2020, 17 EU Member States did so in 2022. We expect this number to continue to increase as new EU Member States are joining the FDI block. That said, over 90% of the deals undergoing EU screening originated from only 6 Member States – Austria, Denmark, France, Germany, Italy and Spain.

The vast majority of notified deals in the EU continue to be cleared unconditionally – 86% in 2022, 73% in 2021, and 79% in 2020. Prohibitions and deal abandonments were limited to 4-5% of the notified deals in 2021 and 2022, a noticeable drop from 9% in 2020, and in line with the Commission's message that the EU is open to FDI and that *"Member States only deny transactions that pose very serious threats to security and public order"*.[8] The remainder (c. 10-20%) of cases required remedies, primarily of a behavioral nature.



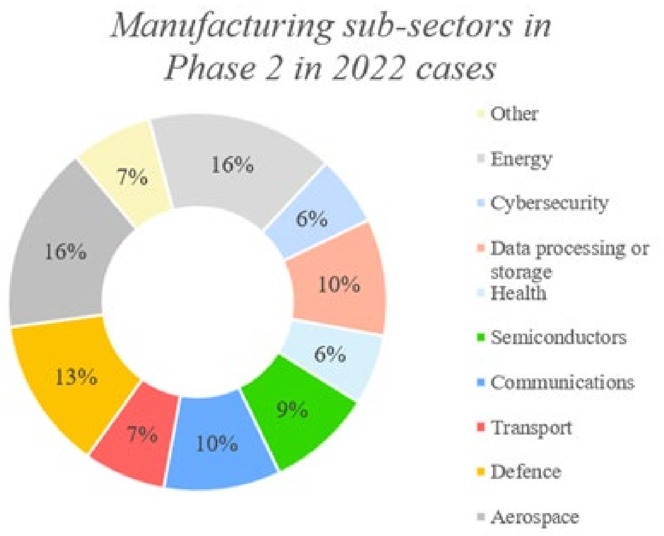
Looking at sectoral trends, the enforcement was mostly directed at manufacturing and ICT sectors, which accounted for two thirds of all in-depth Phase II reviews in 2022 and 2021.



[7] Unlike well-established FDI regimes in the United States, Canada, and Australia, the EU does not have the power to review and authorize foreign investments nor, more generally, act as an overarching regulator. Instead, the EC facilitates the cooperation among Member States screening foreign investments under their national FDI screening processes, and provides views and opinions for the Member States consideration where relevant. In practice, Member States must notify the EC and all other Member States of FDI undergoing screening. The EC or other Member States can intervene if they wish by providing an opinion within a statutory period of 35 calendar days (this normally suspends the course of the national screening). If a third of Member States consider a particular FDI to likely affect security or public order in a Member State or in the EU, the EC must provide its opinion. While such opinion is not binding, this process creates pressure on the host Member State, which should take due account of the EC opinion

[8] *The Report*, p. 13.

Within manufacturing, the EU FDI agencies focused on energy, cybersecurity, data processing and storage, health, semiconductors, communications, transport, defense, and aerospace. This is unsurprising as all of these activities feature prominently in the list of "critical sectors" contained in Article 4 of the EU FDI Regulation.



IV. Semiconductors Deep Dive

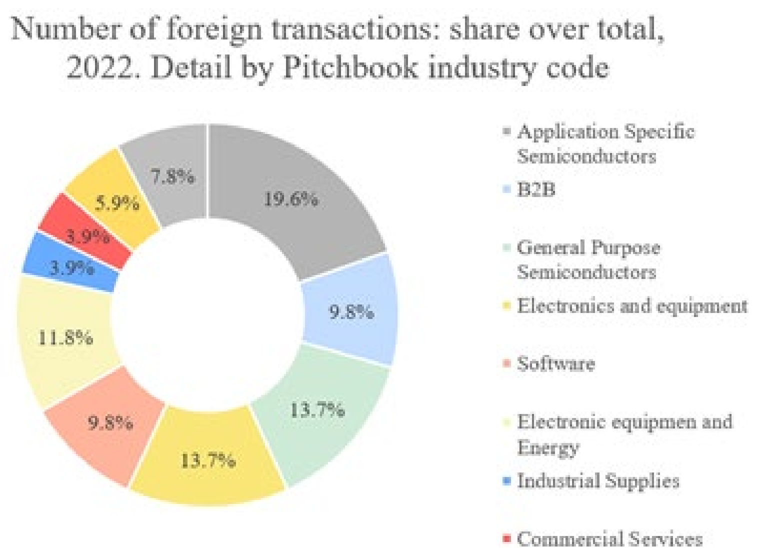
The semiconductor sector has attracted significant FDI scrutiny in Europe in recent years. In order to strengthen its technological supremacy and bolster its competitiveness in semiconductors, the EU passed the European Chips Act (the "**Act**"). Entered into force on September 21, 2023, the Act aims to address semiconductor shortages by unlocking over EUR 43 billion of public and private investments. The Act is composed of three main pillars:

i. The Chips for Europe Initiative, which aims to build large-scale technological capacity and innovation;

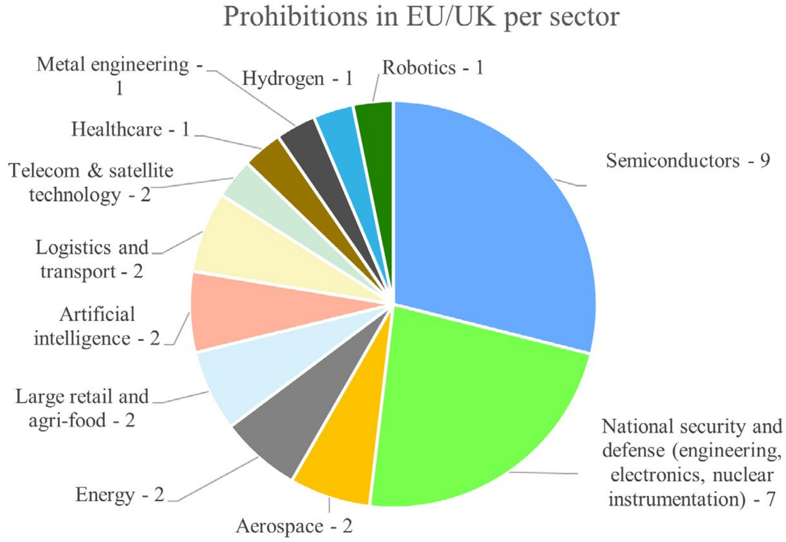
ii. A framework to incentivize public and private investments in manufacturing facilities to secure Europe's supply chains; and

iii. a coordination mechanism between the Commission, Member States and stakeholders.

In line with the regulatory spotlight on semiconductors, EU FDI agencies typically screen investments across the semiconductor chain:



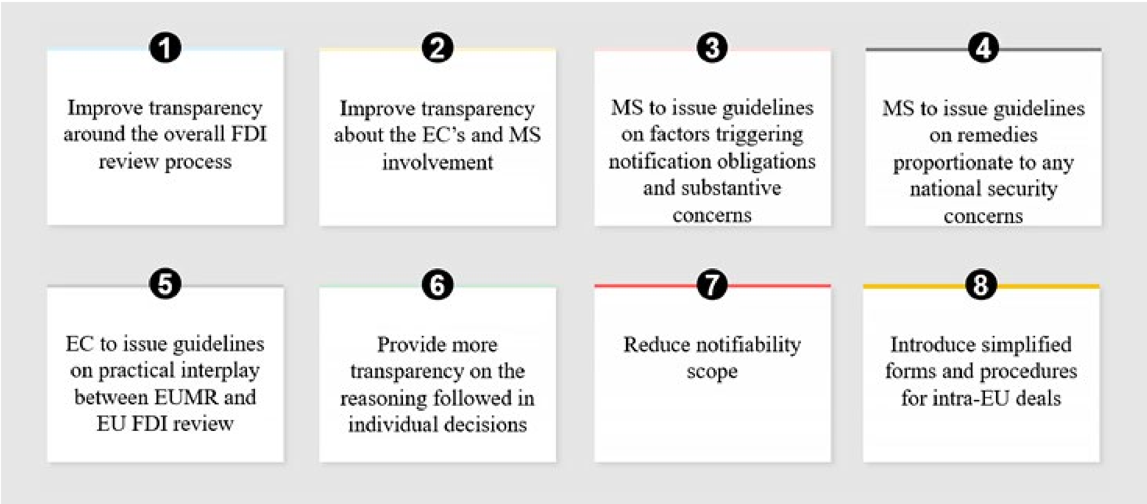
European vigilance on the semiconductor chain is also evident from recent FDI prohibition statistics – one out of every three publicly known deal blocks in the EU/UK in recent years related to semiconductors, and all of those prohibitions related to investors with ties to China.



Recent Prohibitions In The Semiconductor Sector In The EU ***All recent FDI prohibitions in the semiconductor sector in Europe relate to investors from China***	
Nexperia Newport (UK, 2022)	Acquisition of Nexperia, a producer of semiconductors for the automotive and medical sectors, by Wingtech Technology unwound due to national security concerns.
Pulsic Limited (UK, 2022)	Acquisition of Pulsic Limited, a producer of tools for semiconductor chips, prohibited on the basis that the technology could be used in the civilian or military supply chain, or for defense.
HighLight Research Limited (UK, 2022)	Acquisition by SiLight blocked on the basis that HighLight Research's technology could be used to build technological capabilities which may present national risks to the UK.
Elmos Semiconductor (Germany, 2022)	Acquisition of Elmos, a producer of semiconductors for the automotive sector, by Sai Microelectronics blocked due to public order and security concerns.
ERS Electronics (Germany, 2022)	As in Elmos Semiconductors, the German government prohibited the acquisition on the basis of public order and security, as the semiconductor sector is key for Germany's strategic technological sovereignty.
Applied Materials (Italy, 2021)	Acquisition of AM IT, a producer of monocrystalline silicon and semiconductors printing equipment, blocked due to impact on photovoltaic manufacturing capacity and transfer of strategic tech.
LPE (Italy, 2021)	Acquisition of LPE, a producer of epitaxial reactors used in the production of chips, by Shenzhen Invenland blocked due to risk to security of supply and transfer of strategic know-how and tech.
Siltronic (Germany, 2020)	Acquisition of Siltronic, a producer of silicon wafers, by GlobalWafers raised objections, leading to the abandonment of the deal.
Aixtron (Germany, 2016)	Acquisition of 50.1% voting rights in Aixtron, a German electronics manufacturer, by Chinese company Fujian Grand Chip Investment initially secured a certificate of non-objection from the German government. The certificate was later revoked by the German government due to concerns reported to the German authorities by the United States government regarding access to sensitive military technology by China as a result of the acquisition. The acquisition was abandoned following a block in the United States pending the new German review.

V. Future of EU FDI?

The European Commission has launched a consultation to evaluate a possible revision and enhancing of the existing FDI cooperation mechanism set forth in the FDI Regulation. Cleary Gottlieb has submitted its contribution to the consultation,[9] and an additional paper with suggestions to make the FDI review more transparent and predictable, and the filing and procedure more simplified in cases with no *prima facie* national security impact. Cleary Gottlieb's principal recommendations are as follows and summarized in detail in our quarterly FDI newsletter.



VI. Conclusion

Although the regulatory landscape in the EU is becoming ever complex, the EU fundamentally remains open to investment, as expressly stated by the Commission, and as illustrated by the enforcement track record in 2022 – 86% unconditional clearances and only 4-5% deal prohibitions. That said, the statistics released by the Commission do not cover FDI review of intra-EU investments, which exists in a number of EU Member States and has triggered controversies and litigation before EU Courts (C-106/22 Xella) regarding its compatibility with the EU single market rules. Moreover, the number of decisions involving remedies is significant (including in comparison with merger control) and may give rise to questions on the appropriateness and proportionality of some of the commitments.

The EU FDI regulatory landscape will continue to evolve for the foreseeable future - 5 new FDI regimes are expected to be added in 2024, the EU FDI framework awaits at least some reforms in the coming year(s), and there are increasing calls to introduce an outbound FDI control regime. Transactional parties are therefore advised to consider how best to navigate the EU regulatory landscape.

CONTACTS

François-Charles Laprévote
Partner
+32 22872184
fclaprevote@cgsh.com

Vladimir Novak
Associate
+32 22872173
vnovak@cgsh.com

Giancarlo Piscitelli
Associate
+32 2 287 2079
gpiscitelli@cgsh.com

[9] Cleary Gottlieb's Submission to the European Commission's Targeted Consultation On The Evaluation And Review Of The EU FDI Regulation, available here. For a discussion of Cleary Gottlieb's follow-up submission to the Commission, please see our latest FDI Newsletter (August–October 2023), available here.

23.1120.10_112223