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China, Italy, the European Union and the "Belt and Road Initiative"

By Peter Hirst and Alejandro Garcia[1]

China's multibillion dollar Belt and Road Initiative (the "**BRI**") was first launched in 2013 in a bid to connect Asia, Africa and Europe through a series of overland corridors and maritime shipping lanes. Since its introduction, the BRI has made significant progress with 125 countries and 29 international organisations having signed 173 co-operation instruments under the initiative's framework.[2] Between 2013 and 2018, these instruments have led to more than USD 90 billion of Chinese investment.[3]

Hungary was the first European country to sign a BRI-related memorandum of understanding with China in 2015. By 2019, a further 22 European countries had signed BRI co-operation instruments. Ties between China and Europe continue to grow with the latest European countries to sign BRI co-operation instruments being Luxembourg and Italy in March 2019.

Italy is the first member of the Group of Seven major developed economies (most commonly known as the G7) to conclude a BRI co-operation instrument. Accordingly, its involvement in the BRI has attracted significant attention.

The memorandum of understanding concluded by China and Italy

During Chinese President Xi Jinping's visit to Rome on 23 March 2019, the Chinese and Italian governments signed a BRI related memorandum of understanding (the "**China-Italy MoU**"). In summary, the document expressed Italy's desire to strengthen political relations and economic ties with China by increasing co-operation in areas such as policy development, transport, logistics and infrastructure, trade, investment and finance.[4] The China-Italy MoU also expresses the parties' desire to promote regional peace, security, and sustainable development as well as work towards a greener, lower carbon economy.[5]

While a number of factors can explain the Italian Government's conclusion of the China-Italy MoU, the pre-existing backdrop of strong investment and close business relations between China and Italy underpinned by numerous international agreements, is illuminating. Indeed, Italy's signature of the China-Italy MoU can be viewed as a manifestation of a broader treaty practice aimed at increasing Chinese investment in Italy.

Chinese investment in Italy and relevant treaties

The first flagship Chinese investment in Italy took place in 1986, when Air China—the country's flag carrier airline—opened a commercial office in Rome. This happened just a few months after Italy and China signed a bilateral investment treaty (the "**China-Italy BIT**") at the end of January 1985.

The China-Italy BIT—which remains in force today—features a number of important substantive guarantees, including an obligation on the host State to afford "*adequate protection*" to investments. The China-Italy BIT further requires compensation to be paid if an investment is expropriated and also contains a most-favoured-nation clause.[6]

Although the China-Italy BIT entitles investors to pursue claims against a host State through arbitration, this dispute resolution provision is more limited than those found in most modern investment treaties by being restricted to disputes on the amount of compensation due following an expropriation. To date, no disputes have arisen under the China-Italy BIT.

Although it would be far-fetched to conclude that these limitations of the China-Italy BIT had a significant impact on the level of Chinese investment into Italy, investment remained low until the 2000s when it started to rise significantly.

Interestingly, this upward trend coincided with the conclusion of another international treaty with China, this time by the European Union ("**EU**") (of which Italy is a founding member), named the 2003 EU-China Comprehensive Strategic Partnership (the "**EU-China CSP**").[7] In support of the EU-China CSP, both sides released policy papers that emphasised the importance of their trade relations. The EU's policy paper stated that "*the EU and China have an ever-greater interest to work together as strategic partners to safeguard and promote sustainable development, peace and stability*".[8] China, on the other hand, laid down policy objectives, such as promoting a sound and steady development of China-EU political relations, fortifying economic co-operation and trade, promoting common development, and expanding cultural and individual exchanges.[9]

As intended, the EU-China CSP led to a significant increase in trade relations and co-operation between China and EU's Member States, including Italy. Between 2005 and 2018, Chinese investments in Italy reached USD 24.99 billion—the fourth highest in the EU after the UK, Germany and France.[10]

By 2018, China accounted for USD 15 billion of Italian exports,[11] making it Italy's ninth largest export market. In turn, imports from China into Italy in 2018 were worth USD 36 billion.[12]

More broadly, at the EU-level, China constitutes the bloc's biggest source of imports and its second-biggest export market after the United States.13 On average, China and EU countries trade over EUR 1 billion a day.[14]

The advent of the BRI and the current EU regulatory landscape

The launch of the BRI has further increased China's interest in investing in Italy—not least thanks to Italy's port infrastructure which is no doubt a big draw for China. In particular, the port of Trieste in northern Italy is an important entry point for Chinese products into the rest of Europe.[15] During President Xi Jinping's visit to Rome in March 2019, China Communications Construction Company (a State-owned infrastructure group) signed co-operation agreements with the port authorities of Trieste and Genoa.[16] In parallel, China Merchants, a Hong Kong based state-owned company terminal manager, was already in talks to set up a joint venture for a terminal at Trieste.[17]

Chinese interest has also spread into related sectors. For example, in 2018, Italian State-owned ship construction group Fincantieri and China State Shipbuilding Corporation ("**CSSC**") signed a memorandum of understanding with a view to expanding their co-operation into all segments of merchant shipbuilding. By February 2017, these two entities had concluded an agreement for the construction of two cruise ships—a project worth around USD 1.5 billion.[18]

Given the flow of investment and trade between China and Italy, the China-Italy MoU should not necessarily come as a surprise. Whether it has the effect of significantly increasing bilateral investment, however, depends on a multitude of factors. From a legal perspective, there are two main factors to note.

First, since 2013 the EU and China have been negotiating a comprehensive treaty (the "**Investment Agreement**") to replace the 26 pre-existing bilateral investment treaties between China and EU's Member States (including the China-Italy BIT).[19] The purpose of the Investment Agreement is set out in the jointly drafted "EU-China 2020 Strategic Agenda for Co-operation". The document states that the Investment Agreement is aimed at providing "*strong protection*" to investors and their investments as well as promoting more predictable long-term access to EU and Chinese markets.[20]

No drafts of the planned Investment Agreement have been made public and all that is known at present comes from statements by the parties in particular the EU. What is clear from these statements is that the Investment Agreement is likely to be significantly more comprehensive than the relatively laconic China-Italy BIT.

At previous talks in November 2018 and February 2019 on the Investment Agreement, it was reported that China and the EU discussed provisions on expropriation and compensation, fair and equitable treatment, sustainable development (i.e. investment-related considerations over the environment and labour), and dispute settlement for investor-State and State-to-State disputes, as well as concerning the freedom of transfers and liberalisation of capital movement related to foreign direct investment.[21] No specific update was provided on these topics following the summit on the EU-China 2020 Strategic Agenda for Corporation in April 2019 but discussions are reported to be progressing steadily.[22]

Principally owing to developments in the EU, it is difficult to predict the eventual form of these specific provisions of the Investment Agreement. In recent years, a number of EU Member States, including Italy, have been at the receiving end of numerous investment treaty claims. Investors have sued Italy at least nine times, most regularly under the Energy Charter Treaty (the "**ECT**"). Italy's first defeat in an ECT claim came in December 2018 in *Greentech Energy Systems A/S v Italy*. Elsewhere, treaty investors have sued Spain in excess of 40 times, again mostly under the ECT, and the Czech Republic 38 times.

This flurry of litigation has led some EU Member States, including Italy, to seek restrictions to the role of investment treaty protection. On 31 December 2014, Italy notified of its withdrawal from the ECT, making it the first ever full ECT Member State to withdraw from the treaty. Although Italy's withdrawal took effect on 1 January 2016, Article 47(2) of the ECT means existing investments in Italy continue to be protected until 1 January 2036.

In light of these developments, there is a good likelihood that the Investment Agreement may contain fewer protection guarantees than those found in some of the pre-existing BITs between Chinese and individual EU Member States. This could lead to a chilling effect on Chinese investment into the EU.

The second and possibly more important legal factor that may prove pivotal to the BRI's success in Italy relates to the regulatory environment. Chinese State-owned or State-controlled companies are increasingly investing in the EU's "critical" infrastructure. Entities partially or wholly owned by the Chinese government own at least four major airports, six seaports and windfarms in at least nine EU countries.[23] This includes China Ocean Shipping Company Limited's takeover of a terminal in Zeebrugge, Belgium and the Greek port of Piraeus at a cost of USD 1 billion.[24]

Chinese companies have also invested in EU technology companies such as Beijing's NAV Technology Co Ltd's 2015 acquisition of Sweden's Silex Microsystems, which manufactures sensors for handsets, cars, and medical devices.[25] This was followed in 2016 by Chinese appliance maker Midea buying German robotics group Kuka. Most recently, Chinese car maker Zhejiang Geely

Holding Group Co gained a nearly 10% stake in Germany's automotive giant Daimler in 2018.[26] It has been reported that owing to Chinese investments being made in "critical" or "sensitive" sectors, some EU Member States, and in particular Germany and France have advocated more stringent screening criteria for foreign direct investments.[27]

Apparently in response to these concerns, on 5 March 2019, the Council of the EU—one of the EU's main decision-making bodies—adopted Regulation (EU) 2019/452 which established a framework for the screening of foreign direct investments into the EU (the "**Screening Regulation**"). According to the Screening Regulation, security screening is necessary in a number of areas including: food supply, energy and raw materials; access to sensitive information such as personal data; critical infrastructure such as transport, energy, water, communication, defence; critical technologies such as artificial intelligence, robotics, cybersecurity, aerospace, nano and bio technologies; and the freedom and pluralism of the media.

Furthermore, if an investment concerns several EU Member States, or if an investment could affect a project or programme of interest to the whole EU (such as Galileo[28] or Horizon 2020[29]), then the EU Commission will be empowered to issue opinions on the admission of the investment.[30]

The Screening Regulation thus grants significant powers to EU bodies and has the potential to significantly impact upon Chinese investment into Italy and elsewhere in the EU. How much it will impact such investments will ultimately depend on how the screening process is implemented in practice.

What the future holds

Given the many factors at play, it is difficult to predict whether the conclusion of the China-Italy MoU will lead to an increase in Chinese investment into Italy and the wider EU, particularly in the long term. Recent data seems to suggest that the signing of the China-Italy MoU has bolstered Chinese investment in Italy. In April 2019, it was reported that Chinese investors signed 29 separate deals in Italy amounting to USD 2.8 billion worth of projects. Whether this upward trend will continue is likely to be influenced by other factors, in particular the application of the Screening Regulation, which could have a dampening effect.

At present, there remain more questions than answers. How these questions are answered may well determine the future of Chinese investment in the EU for years to come. Only time will tell if the BRI's road is broadening or narrowing and its belt is loosening or tightening.

[1] Peter Hirst is the Co-Chair of the Global Arbitration Group of Clyde & Co (London) and a Professor of Law at the University of Aberdeen. Alejandro Garcia is a partner at the Global Arbitration Group of Clyde & Co (London). The views in this article are the authors'. The authors thank Francesca Fraser and James Newton of Clyde & Co for their assistance.

[2] https://www.telegraph.co.uk/china-watch/business/belt-road-projects-list/

[3] http://www.globaltimes.cn/content/1141188.shtml

[4] http://www.governo.it/sites/governo.it/files/documenti/documenti/Notizie-allegati/Italia-Cina_20190323/Memorandum_Italia-Cina_EN.pdf

[5] http://www.governo.it/sites/governo.it/files/documenti/documenti/Notizie-allegati/Italia-Cina_20190323/Memorandum_Italia-Cina_EN.pdf

[6] A provision ensuring that the host State extends any better treatment afforded to third parties to investments protected under the BIT.

[7] Cf. Document "EU-China 2020 Strategic Agenda for Co-operation", p. 2, available at: http://eeas.europa.eu/archives/docs/china/docs/eu-china_2020_strategic_agenda_en.pdf

[8] EU Commission Policy Paper, "A maturing partnership - shared interests and challenges in EU-China relations", COM/2003/0533 final, available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:52003DC0533

[9] The text of the China's "EU Policy Paper" of October 2003 is available at: http://gr.china-embassy.org/eng/zgyom/

[10] http://www.aei.org/china-global-investment-tracker/

[11] http://www.worldstopexports.com/italys-top-import-partners/

[12] http://www.worldsrichestcountries.com/top-italy-imports.html

[13] http://ec.europa.eu/trade/policy/countries-and-regions/countries/china/index_en.htm

[14] http://ec.europa.eu/trade/policy/countries-and-regions/countries/china/index_en.htm

[15] Autorita' di Sistema Portuale del Mare Adriatico Orientale (AdSP – Eastern Adriatic Sea Port Authority) and state-owned China Communications Construction Company have signed an agreement to develop the port's infrastructure and to increase access for products of small and medium-sized Italian companies into Chinese markets: https://www.portseurope.com/trieste-port-signs-agreement-with-china-communications-construction-company/

[16] In total, Chinese investors signed twenty-nine separate deals amounting to USD 2.8 billion worth of projects: http://www.globalconstructionreview.com/news/china-eyes-trieste-and-genoa-italy-joins-chinas-be/

[17] https://www.scmp.com/news/china/diplomacy/article/3002305/italy-may-be-ready-open-four-ports-chinese-investment-under

[18] https://www.fincantieri.com/en/media/press-releases/2018/fincantieri-progress-in-the-chinese-projects/

[19] http://ec.europa.eu/trade/policy/countries-and-regions/countries/china/index_en.htm

[20] Cf. EU-China 2020 Strategic Agenda for Co-operation, adopted by both Parties at their 16th summit in 2014, p. 5, available at: http://eeas.europa.eu/archives/docs/china/docs/eu-china_2020_strategic_agenda_en.pdf

[21] Report of the 20th round of negotiations for the EU-China Investment Agreement on 1 March 2019, available at: http://trade.ec.europa.eu/doclib/docs/2019/march/tradoc_157772.pdf; Report of the 19th round of negotiations for the EU-China Investment Agreement of 13 November 2018, available at: http://trade.ec.europa.eu/doclib/docs/2018/november/tradoc_157495..._.pdf

[22] https://www.voanews.com/a/china-eu-agree-to-strengthen-trade-relationship/4868431.html

[23] https://www.bloomberg.com/graphics/2018-china-business-in-europe/

[24] https://foreignpolicy.com/2018/02/02/why-is-china-buying-up-europes-ports/

[25] https://www.bloomberg.com/news/articles/2018-11-29/chinese-takeover-of-eu-tech-assets-set-for-greater-scrutiny

[26] https://www.ft.com/content/37fe00c0-14e1-11e9-a581-4ff78404524e

[27] https://www.ft.com/content/04fa752c-7dda-11e7-ab01-a13271d1ee9c; https://www.ft.com/content/17f91d24-3f60-11e9-b896-fe36ec32aece.

[28] Galileo is Europe's £8bn Global Navigation Satellite System (GNSS). The system is intended to rival the US-controlled Global Positioning System. Once fully operational in 2020 it will provide accurate position, navigation and timing information to be used by governments, citizens and industry. It will be used by everything from smartphones to security-critical military applications in target acquisition and tracking: https://www.gsa.europa.eu/european-gnss/galileo/galileo-european-global-satellite-based-navigation-system and https://www.theguardian.com/politics/2018/may/25/what-is-galileo-and-why-are-the-uk-and-eu-arguing-about-it

[29] Horizon 2020 is the biggest EU Research and Innovation programme ever with nearly EUR 80 billion of funding available over 7 years (2014 to 2020). It is a collaborative financial instrument with the aim of putting Europe at the heart of world class science and innovation, making it more competitive, creating growth and new jobs: https://ec.europa.eu/programmes/horizon2020/what-horizon-2020

[30] http://europa.eu/rapid/press-release_IP-19-1052_en.htm

Authors

If you would like further information on any issue raised in this update please contact:

Peter Hirst
Senior Partner Elect
T: +44 20 7876 4425
E: peter.hirst@clydeco.com

Alejandro Garcia
Partner
T: +44 20 7876 6529
E: alejandro.garcia@clydeco.com