Executive Summary: Chinese investors' confidence report under the context of CAI

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Purpose and methodology of the survey

On 30 December 2020, the leaders of China, Germany, France and the European Union ("EU") jointly announced the completion of the negotiation of the China-EU Comprehensive Agreement on Investment ("the Agreement" or "CAI") in a video conference.

To take an in-depth look at the impact of the Agreement on China-EU bilateral investment and industry development and assessment and expectation of enterprises in relation to how the Agreement will develop, PwC was engaged by China Council for the Promotion of International Trade ("CCPIT") to conduct an enterprise feedback survey in 2021. In the nearly three-month long survey, PwC collected a questionnaire targeting mainly domestic enterprises, as well as certain representatives of foreign companies in China, experts and scholars, in combination of expert interviews and discussions with enterprises.

The report is a collation of 512 valid responses from enterprises in manufacturing, non-financial services, financial services, agriculture and other sectors from 11 provinces and municipalities, including Beijing, Shanghai, Shandong and Jiangsu. The main findings and relevant recommendations set out in the Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment ("the Report") are the fruits of the survey, and are evidenced by feedbacks from businesses.

Snapshot of Recent Trade and Investment between China and EU

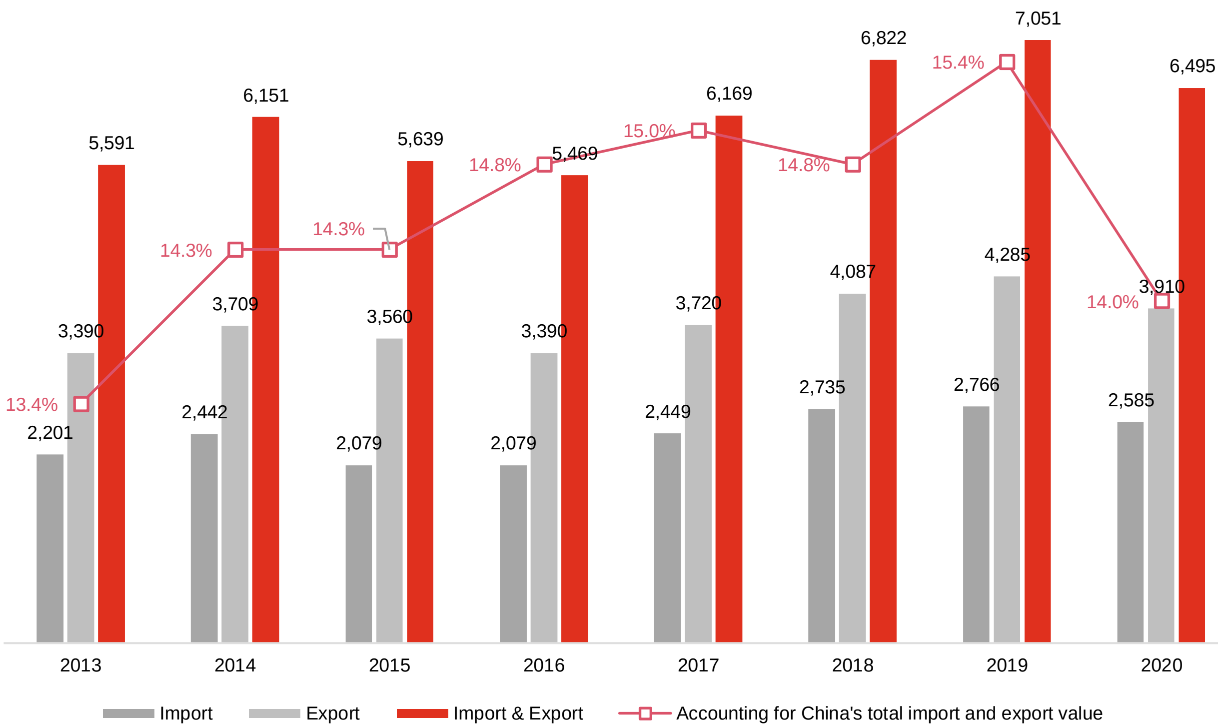
In May 1975, China and the EU formally established diplomatic relations, and since then bilateral relations have been continuously injected with new vitality and given new connotations. In the past 46 years, China and the EU have continuously deepened their partnership in line with the principle of mutual respect and harmonious coexistence, from long-term partners and comprehensive partners to comprehensive strategic partners, and bilateral cooperation has expanded from economic and trade to peace and security, environment, science and technology, culture, education, health and many other fields, and pragmatic cooperation has achieved remarkable results.

Trade in goods is mutually dependent.

The EU has been China's largest trading partner for many years, and China has firmly ranked as the EU's second largest trading partner. In 2020, trade in goods between China and the EU bucked the trend by 4.9%[1] to US$649.5 billion, accounting for 14% of China's total foreign trade in the context of a sharp contraction in global trade, China surpassed the United States to become the EU's largest trading partner, and the EU is China's second largest trading partner.

Note1: The prior year base does not cover the UK

Trade in goods between China and the EU in 2013-2020 (US$100 million)[2]



Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

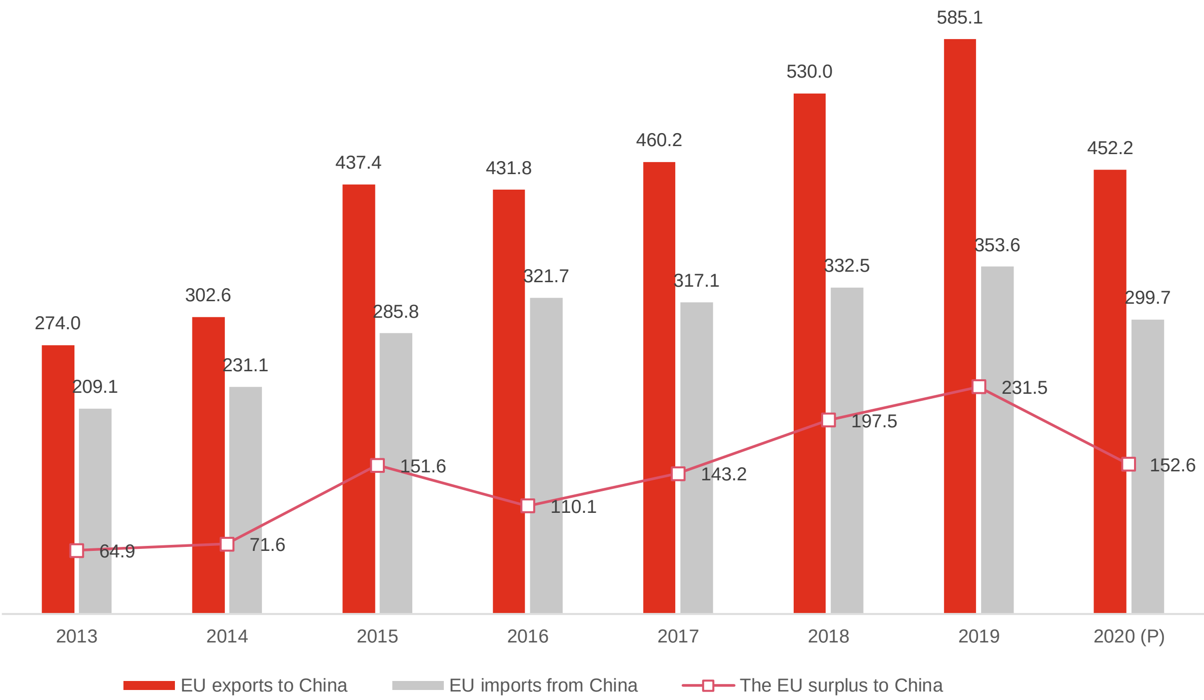
Note2: The figures from 2013 to 2019 included UK, 2020 did not include UK due to Brexit

The service trade has great potential.

At present, the base of China-EU service trade is small, and the overall trend is growing, and has a large space for development.

For China, trade in services to the EU has been in a deficit, and the growth rate of exports has not been as fast as the growth rate of imports. In the future, for China, we can use our own advantages to increase exports of services to Europe, including emerging service exports represented by digital services.

Trade in services between China and the EU in 2013-2020 (EUR€100 million)



Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

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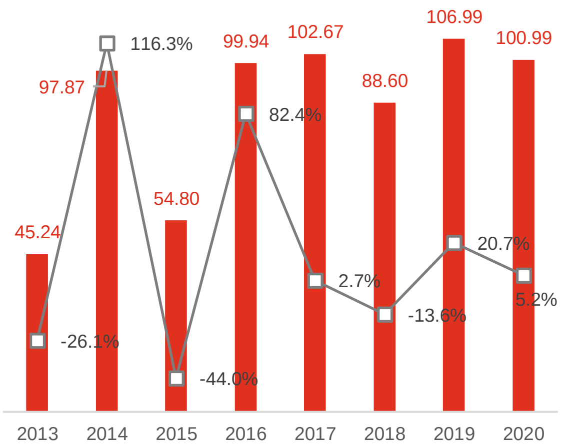
Bi-lateral direct investment between China and EU is still not so great.

After the establishment of a comprehensive strategic partnership between China and the EU, two-way investments have become more active. In 2016, China's direct investment in the EU increased by about 82% year-on-year, and EU direct investment in China increased by 35.2% year-on-year, achieving a significant increase. Since then, there has been no substantial breakthrough in two-way investment between China and the EU.

In 2020, China's direct investment in the EU was US$10 billion, an increase of 5.2% year-on-year. EU direct investment flows to China were US$5.7 billion, down 11.8% year-on-year. In absolute terms, the level of two-way investment between China and the EU is still not great, which does not match the size of trade and the volume of the economy between the two sides.

China's direct investment flows to the EU (US$100 million) and year-on-year growth rate from 2013 to 2020



Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

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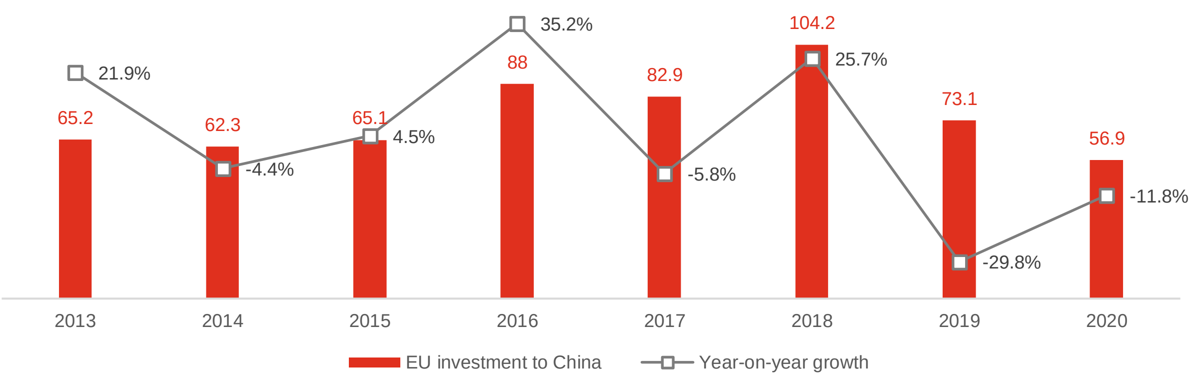
EU direct investment flows to China (US$100 million) and year-on-year growth rate in 2013-2020



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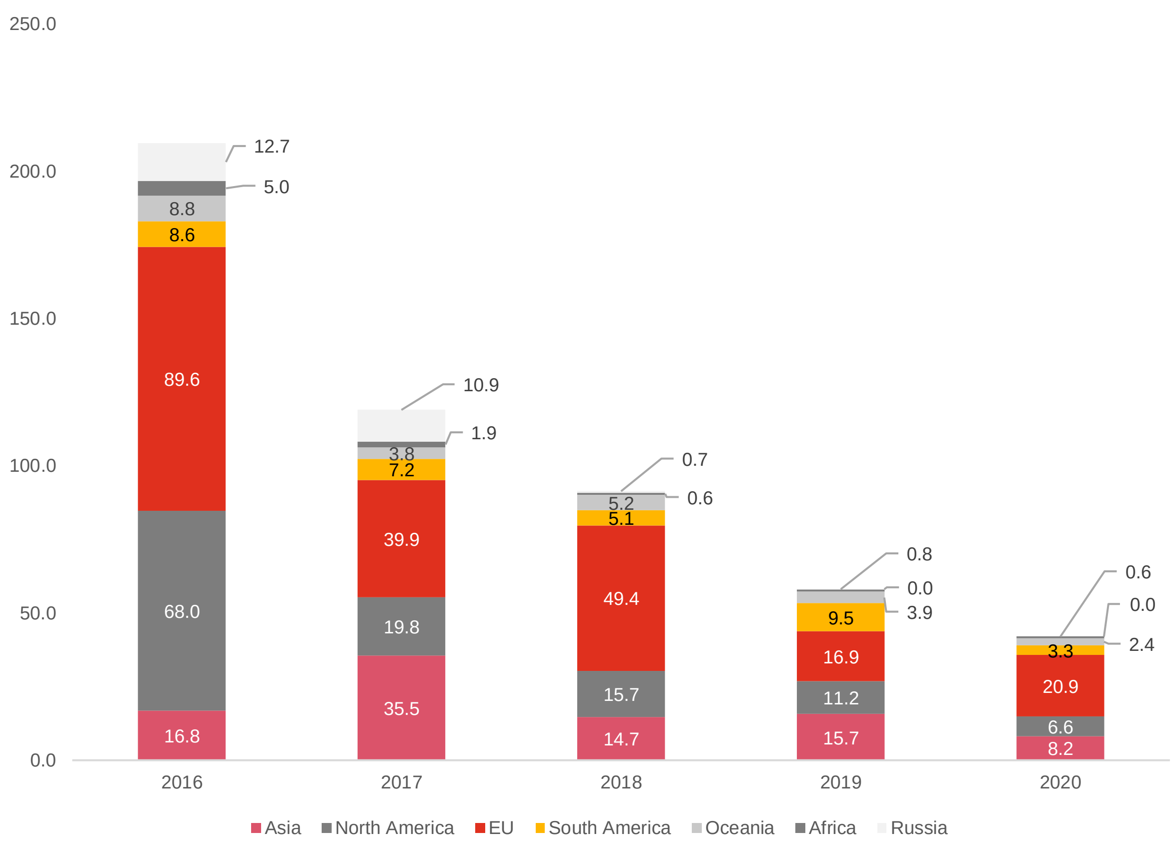
In the past three years, the M&A transactions of Chinese enterprises in Europe have shown a downward trend.

Affected by events such as the epidemic and Brexit, the number of M&A transactions of Chinese enterprises in Europe has declined year by year in the past three years. In 2020, the overall amount of European M&A by Chinese companies was US$2.09 billion.

The amount of overseas M&A by Chinese enterprise (US$100 million) by investment region



Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

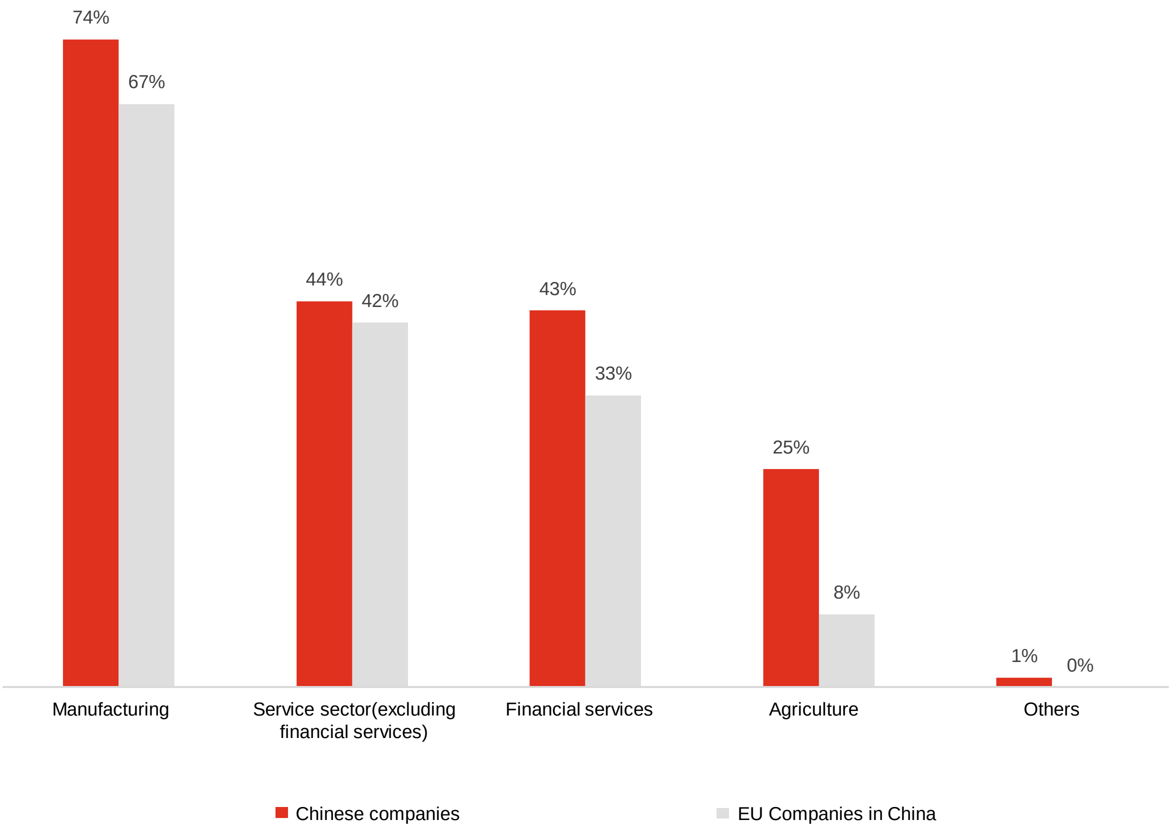
Chinese – EU Investors' Survey Key Findings

In general, the business circle is looking forward to the conclusion of CAI and believes that CAI will bring new opportunities to bilateral investment and industry development.

Before the signing of the Agreement, some companies are waiting to see the outcome, while others consider getting prepared for the possible short-term impact in terms of strategic planning, core competitiveness enhancement, cultivation of international high-end talents, etc.

According to the survey, 74% of the Chinese companies surveyed believe that the CAI will be beneficial to the development of their own manufacturing industry, and the share of EU companies surveyed is 67%.

Expected benefits which the signing of CAI will bring to various industries

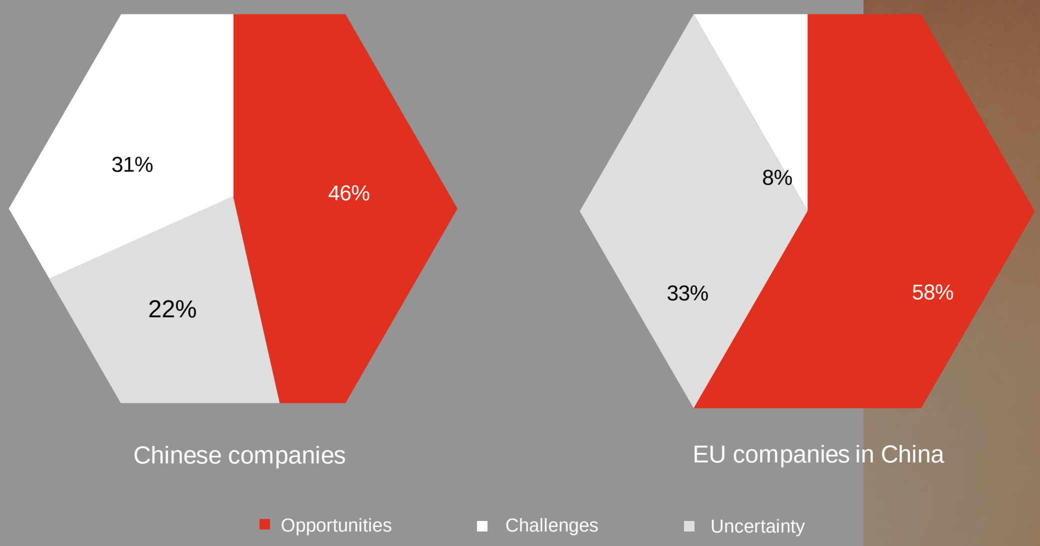


Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

The opportunities of China-EU bilateral investment presented by CAI outweigh challenges.

According to the survey, 46% of the Chinese enterprises surveyed and 58% of the EU enterprises surveyed believe that the signing and the enforcement of CAI will have a positive impact on bilateral investment between China and the EU, and enterprises will benefit from it.

Expectation on the impact of CAI on China-EU bilateral investment



01 It is beneficial for EU automotive, finance, medical, telecommunications, computer and other fields to enter into the Chinese market.

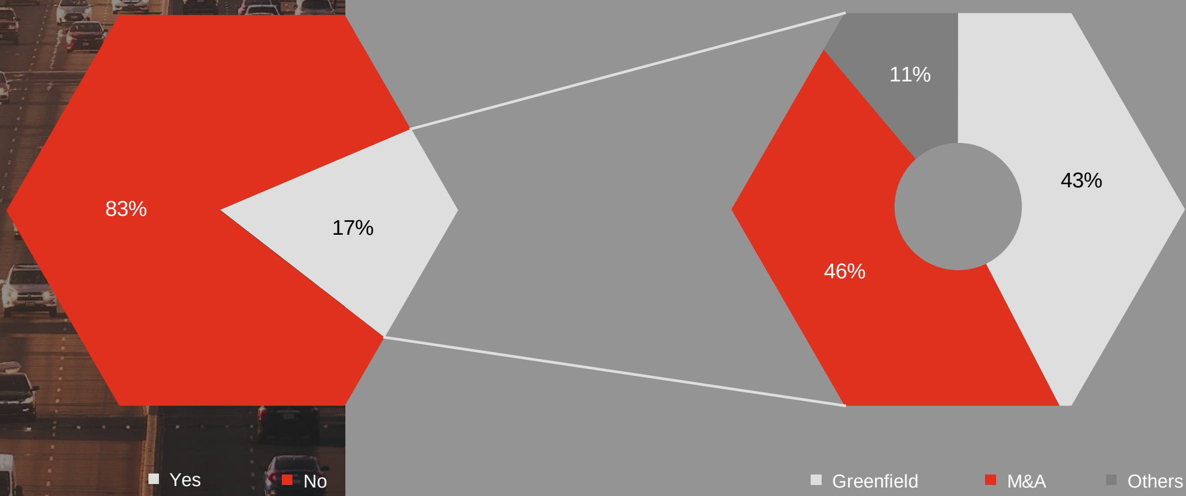
02 It is beneficial for Chinese enterprises in the sectors of new energy, environmental protection and electronics industry to invest in the EU.

Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

Companies surveyed investing in the EU mainly through M&A and Greenfield.

According to the survey, 17% of the Chinese respondents have invested in the EU. Among them, 46% invested in the EU through mergers and acquisitions, and 43% of enterprises have been doing greenfield investment, which is apparently a growing trend.

Companies surveyed investing in the EU status quo

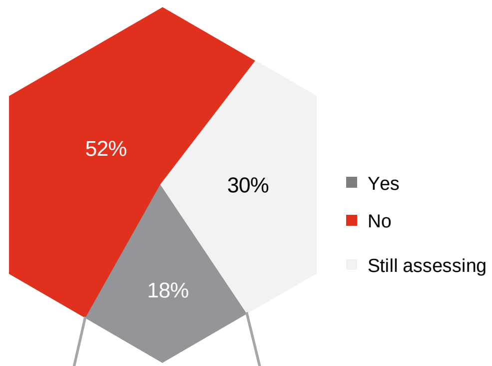


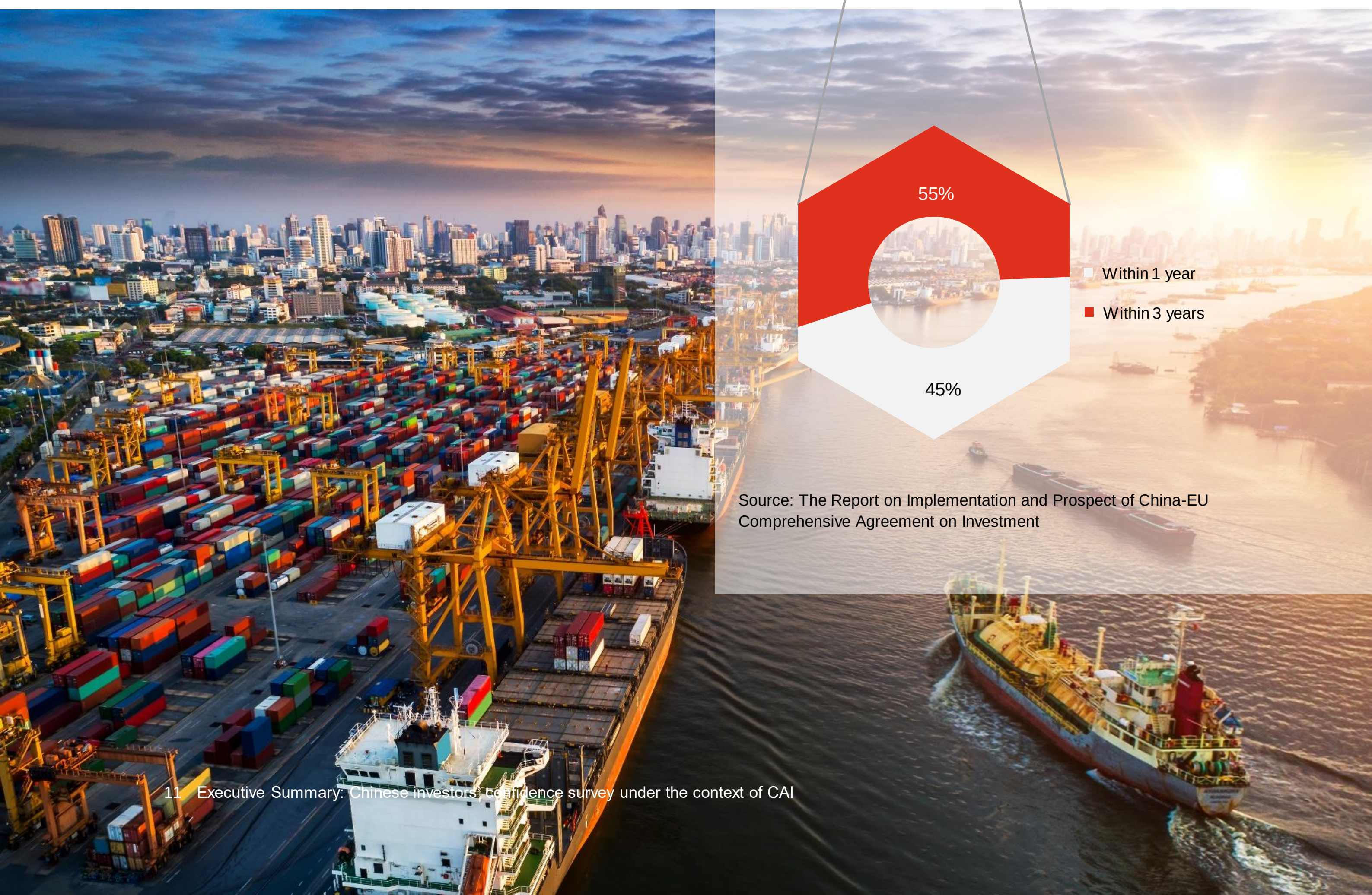
Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

In the future, Chinese enterprises have a large room for growth in investment in the EU.

According to the Survey, 48% of respondents will consider investing in EU within 3 years; while 18% confirmed will invest in the EU. There are 30% of respondents are assessing the dynamics and opportunities in investing in the EU, reflecting the big room for Chinese investment in the EU. The signing and entry into force of a high-level investment agreement is particularly important for further unleashing the potential of investment in Europe.

Companies surveyed recent investment plans in the EU





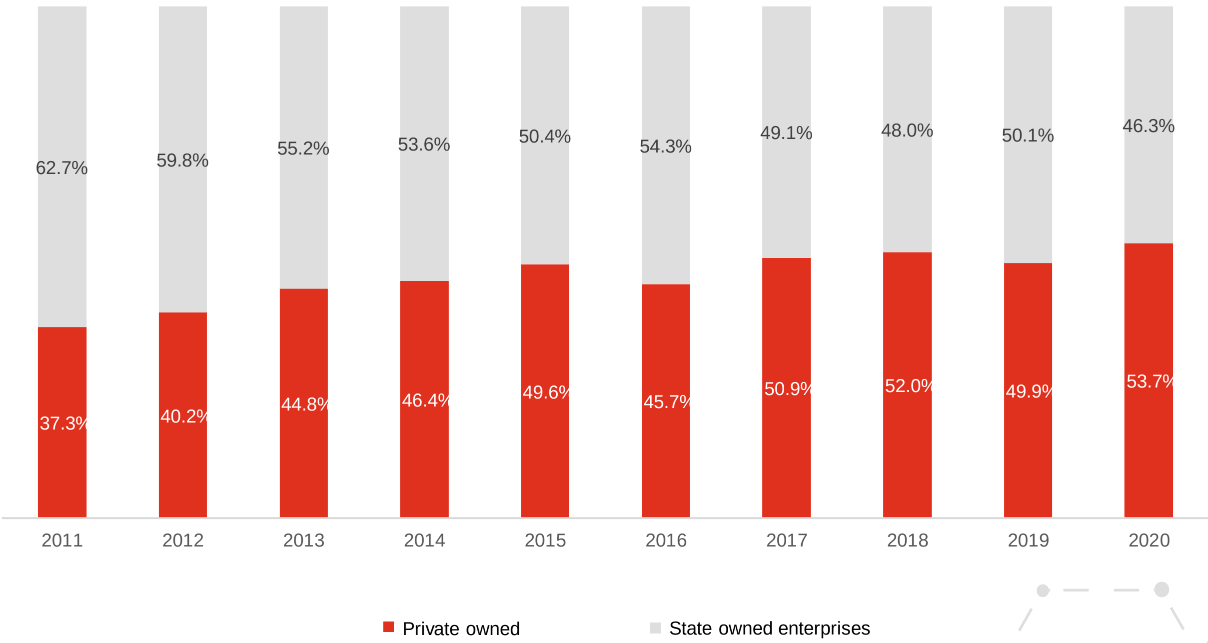
Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

Privately owned enterprise is the major driver of Chinese investments.

Among the surveyed enterprises that have invested in the EU, private and private holding enterprises are the majority, accounting for 67%.

Most of private owned enterprises are located in Eastern Coastal region of China, including Zhejiang, Jiangsu, Guangdong and Shandong provinces. Chinese POEs are out-investing SOEs in outbound investment activities in recent years which is reflecting the desire of private businesses to expand their oversea businesses. This may also represent opportunities for European businesses looking for capital investments.

Distribution of China's Outward Non-financial Direct Investment Stock by Domestic Investor Registration Type at the End of 2020



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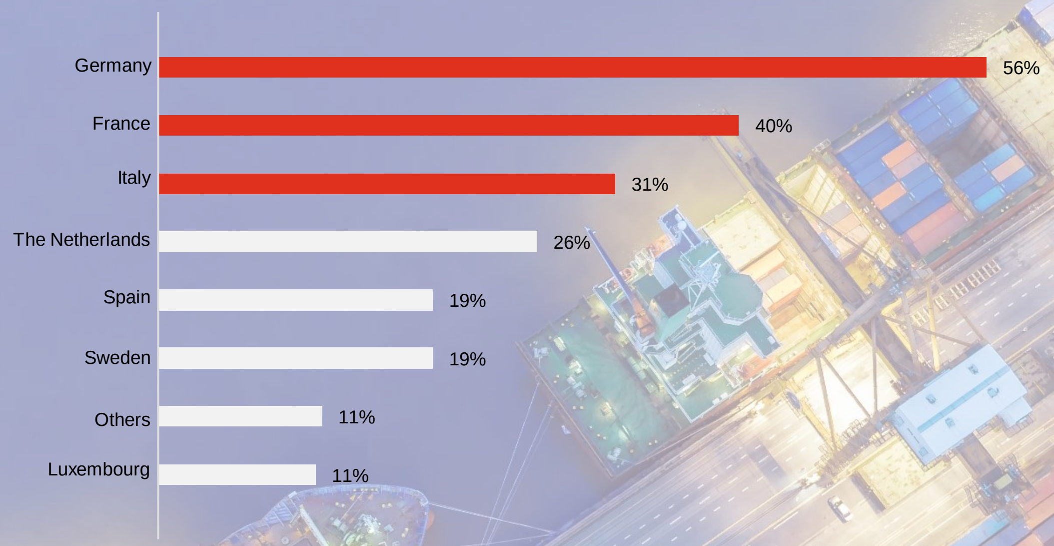
Note: The figures did not include financial services enterprises

Germany, France and Italy are the top 3 most attractive destinations for investments.

Among Chinese companies with investment plans for the EU, 56% plan to invest in Germany and 40% in France. In addition, 31% and 19% of the surveyed companies said they planned to invest in Italy and Spain, respectively. Compared with Germany and France, the investment environment in southern European countries is relatively less affected by political factors and is becoming an important target for Chinese enterprises to invest in Europe and expand their business territory.

Planned destinations of investment in the EU for Chinese companies surveyed

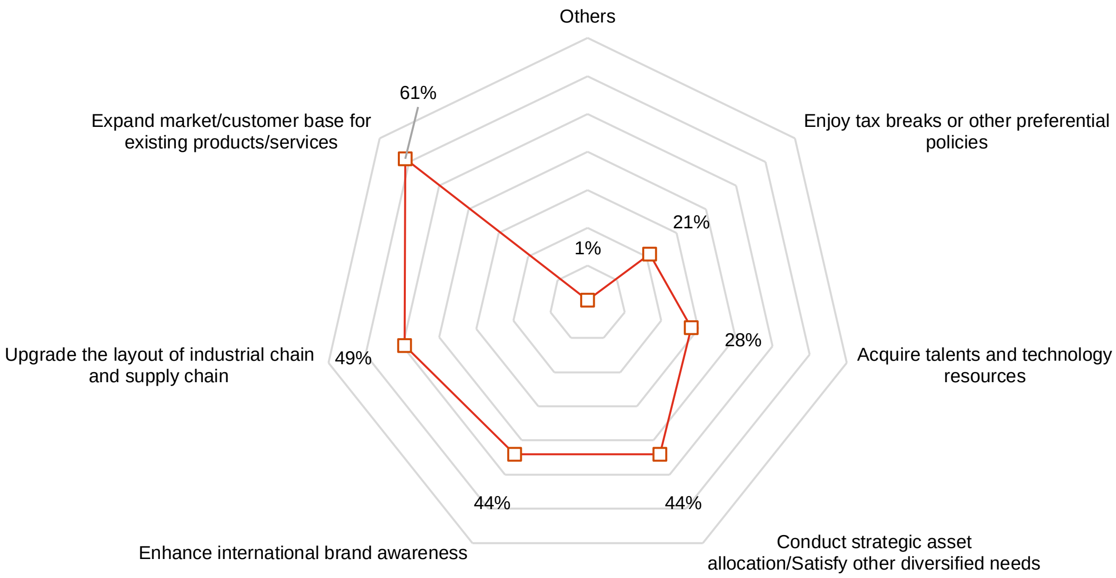


Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

The main drivers of Chinese investment in the EU are market access and the demand for an upgraded industrial chain.

According to the existing and prospective Chinese investors in the EU surveyed, 61% of them were intended to get access to EU market and expand customer base for their existing products or services; 49% hoped to upgrade their layout of industrial chain and supply chain through investment; 44% aimed to enhance international brand awareness; 44% were meant to conduct strategic asset allocation or satisfy other diversified needs; and 28% wished to acquire talents and technology resources by investment. Among the companies surveyed with investment plans for the EU, 97% said that they would mainly consider investing in the company's core business and upstream and downstream businesses, and only 3% said they would consider investing in non-core business.

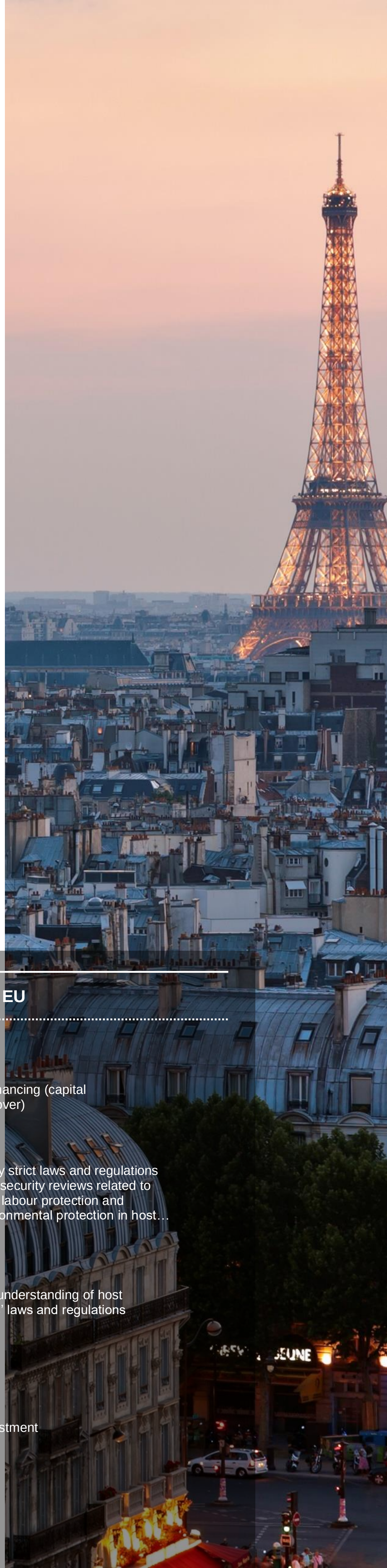
Purposes of investment in the EU for companies surveyed



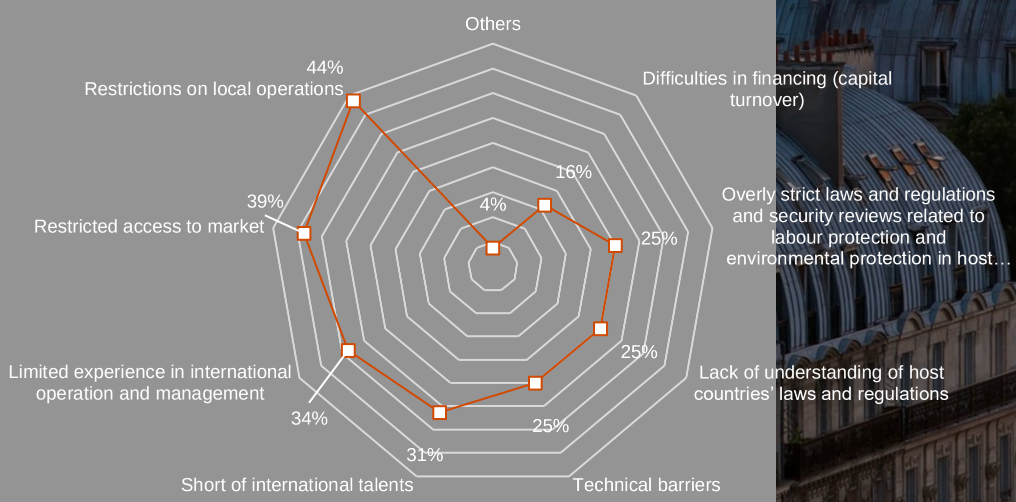
Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

In respect of investment in Europe, Chinese enterprises are still facing with difficulties and looking for more professional services.

The survey indicates that due to market access limitations, licensing requirements and technical barriers are hindering Chinese enterprise from investing in Europe. Among the surveyed companies investing in the EU, 44% said that restrictions on local operations were their main problem, 39% were affected by market access limitations, 25% believed that the laws and regulations and security reviews of host countries were overly strict and 25% had to deal with technical barriers. In the context of a faster adjustment to foreign investment security review policies by the EU, there is robust demand for policy and service support, ranging from management guidance, information service, platform service to risk warning service on corporate compliant operation.



Obstacles and challenges faced by Chinese companies in investing in the EU



Source: The Report on Implementation and Prospect of China-EU Comprehensive Agreement on Investment

Recommendations for Chinese enterprises investing in Europe

The report has set out seven recommendations for Chinese enterprises planning to invest in Europe.

First, closely follow the progress of CAI and develop strategic plans for overseas operations in advance.

It's recommended that new energy, new infrastructure and high-tech enterprises should keep abreast of the discussions of EU and its member states over the Agreement, to come up with plans to "go global" after the Agreement takes effect.

Second, SOEs should properly manage the issues related to competitive neutrality and prudently assess overall risks.

With the entry into force of the CAI in the future, SOEs or state-holding enterprises need to pay special attention to extra limitations imposed by the destinations of investment.

Third, invest more in research and development and put high on the agenda the investment cooperation with the EU in high-tech areas.

While securing investment in traditional key fields including automotive industry, companies should pay utmost attention to scientific and technological innovation, environmental protection, biomedicines, etc in planning their investment.

Fourth, intensify compliance management on environmental protection and labour protection in daily operations and shoulder corporate social responsibilities.

We suggest that companies should practice sustainable development concepts in daily operations, set up sound compliance management mechanisms for environmental protection and labour protection and oversee the implementation of the mechanisms; and incorporate environmental, social and governance (ESG) ideas in business operation and core strategies.

Fifth, foster closer cooperation with local companies in the EU to tap into third-party markets.

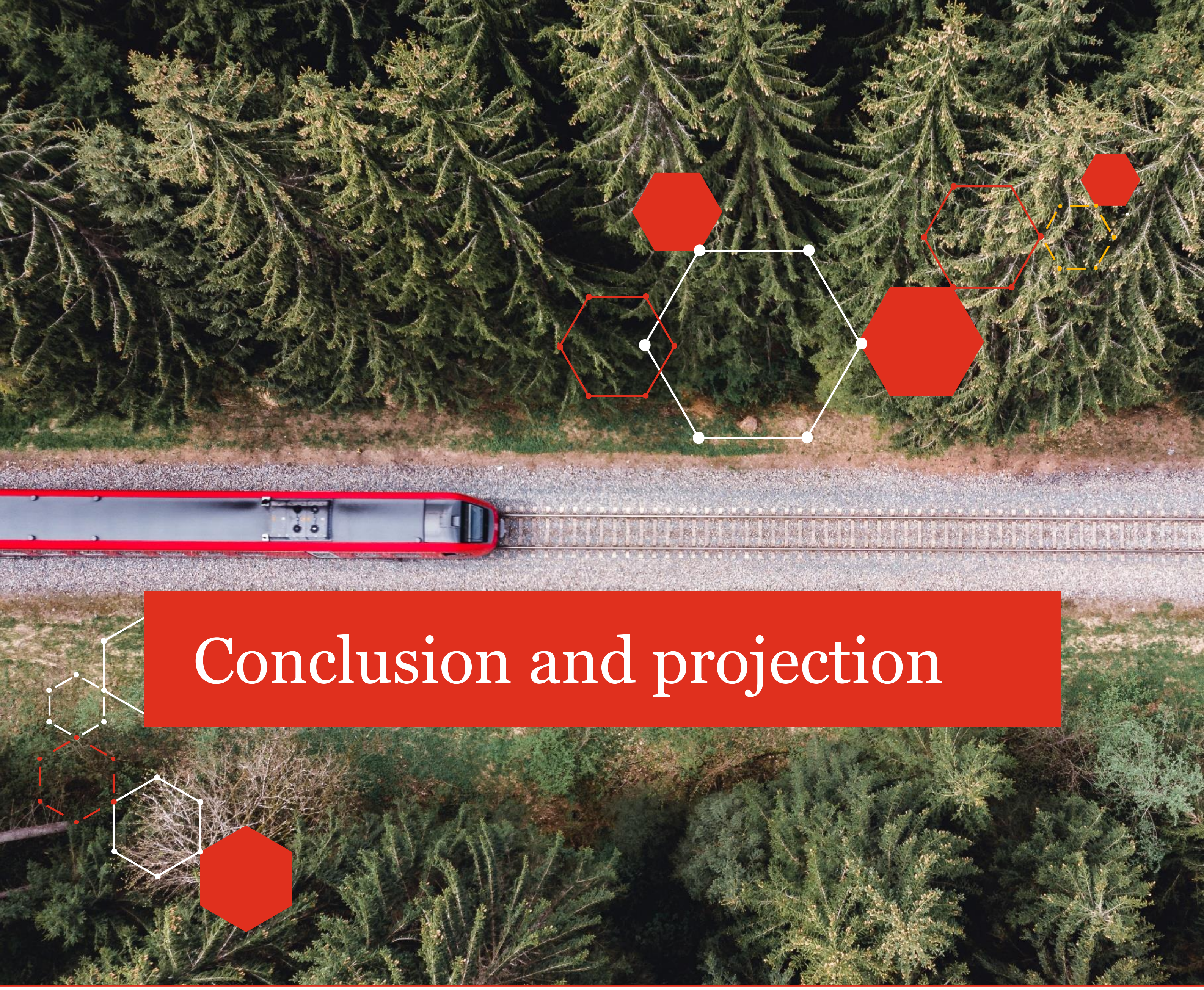
It is clear that China and the EU can complement each other on the economic, industrial and business front. We recommend that Chinese companies hoping to invest in Europe should increase cooperation with local companies in host countries and integrate their own advantage resources to explore third-party markets.

Sixth, cultivate corporate culture upholding diversity and inclusiveness and increase local recognition for Chinese companies.

Companies should get some insights into the business environment and operation mode in the EU, create a diverse and inclusive culture across the company, cope with cross-culture issues brought about by investing in Europe, and try to get recognition from local governments, companies and employees.

Seventh, get prepared for the early stages of investment, improve transparency and effectively respond to foreign investment reviews of the EU.

Pre-investment investigation shall be refined, research on the foreign investment review system of the EU shall be conducted and voluntary disclosures on investment content shall be made to host countries to build further trust with governments and investees of host countries.



Conclusion and projection

In summary, China and Europe are key trading and investment partners to each other. The huge potential of China-EU economic and trade cooperation is the main driving force for the initiating and finalising of CAI negotiations. The EU-China investment deal is facing certain hurdles, however, the business community in both China and Europe are expecting something from the Agreement, as the incentive to achieve mutual benefits through cooperation and the trend to a better China-EU relation will not change fundamentally.

So far, there has been great uncertainty in the global economic recovery, whereas China-EU economic and trade cooperation demonstrates robust resilience. Looking forward, the bilateral cooperation enjoys promising prospects and an intensified one is surely a popular trend that cannot be reversed. If the Agreement can be concluded in a foreseeable future, it will become a power driver for in-depth China-EU economic and trade cooperation and bring tangible benefits to social and economic development, industrial transformation, and upgrading business internationalisation on both sides.

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