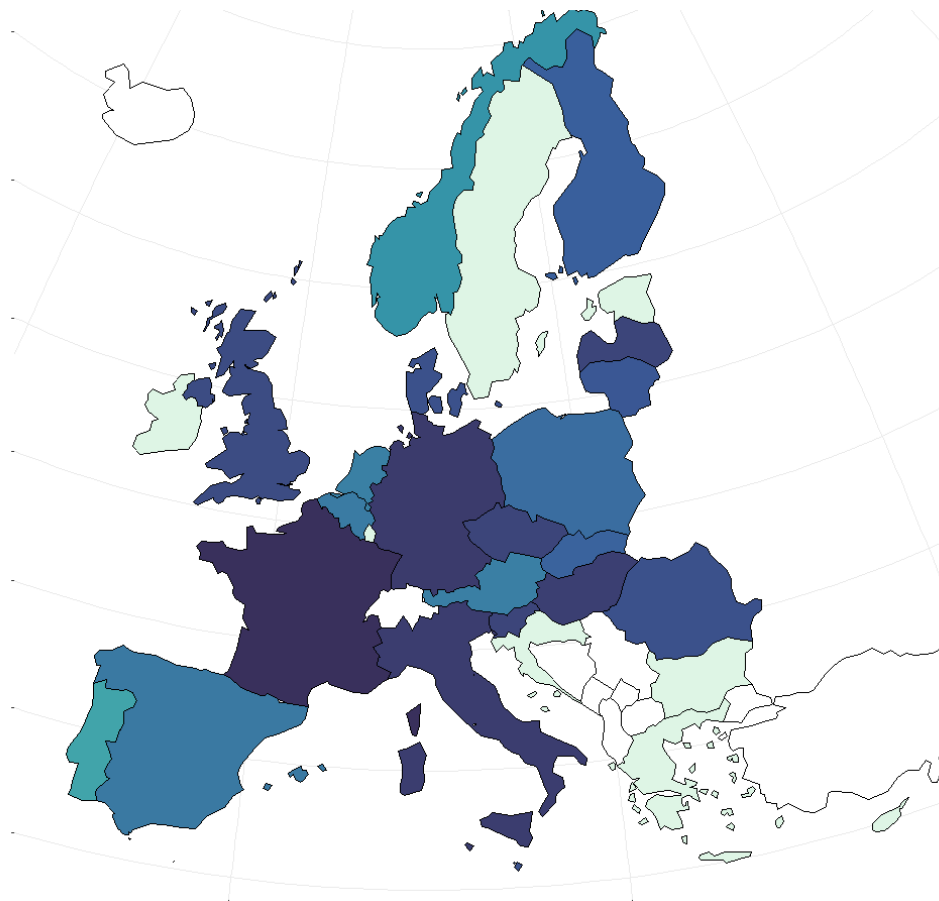


# The rise in FDI screening in the EU and major advanced economies

Lorenzo Bencivelli, Violaine Faubert, Florian Le Gallo, Pauline Négrin

*In order to meet national security concerns, many advanced economies, particularly in Europe, have adopted or strengthened their mechanisms for screening inward foreign investment. The extent of this screening varies from country to country, including within the EU. However, advanced economies remain open to investment.*

Chart 1: Restrictiveness of foreign investment screening mechanisms (ISMs) in Europe



*Note: the darker the blue, the more restrictive the ISM. Member States that have initiated a process to adopt an ISM are shown in green.*

*Source: [Bencivelli et al., 2023](#)*

## FDI screening, a mechanism to address national security concerns

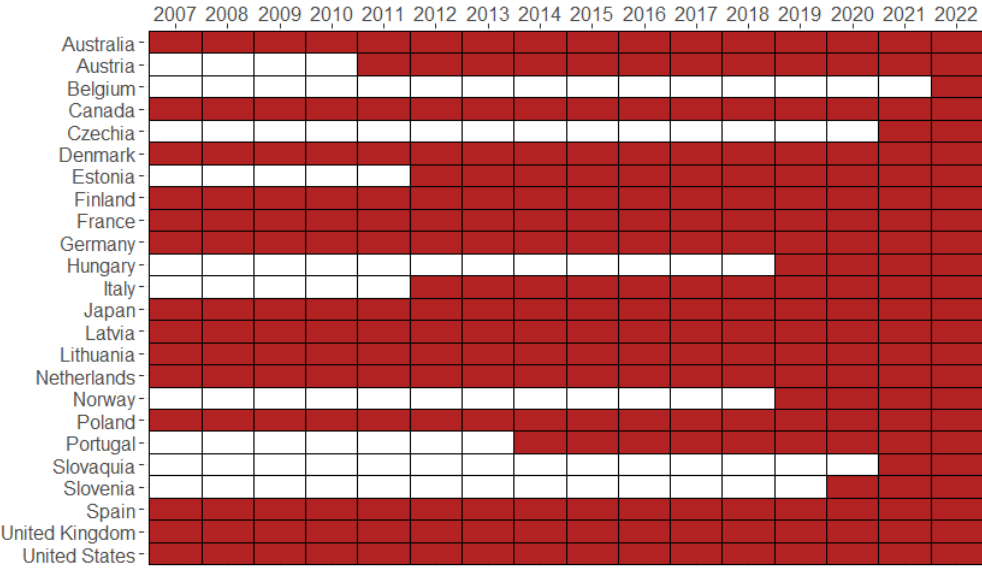
Over the last decade, although most advanced economies have traditionally been open to foreign investment, they have adopted or strengthened their investment screening mechanisms (ISMs).

These mechanisms enable national authorities to examine, authorise subject to conditions, or even prohibit transactions likely to threaten national security, particularly in strategic sectors (critical infrastructure or technologies, energy, health, media, etc.), or when investors are controlled by the government of a third country.

First introduced in the 1970s and 1980s in the United States, Canada and Australia, ISMs have more recently been introduced in Europe (see Chart 2). Although most ISMs apply to all foreign investors, irrespective of their nationality, their diffusion can be seen as a response to the surge in investment from emerging economies to advanced economies in the 2010s ([Bauerle and Meunier, 2023](#)). ISMs are being strengthened in line with the increasing consideration of geopolitical factors in economic decision-making ([IMF 2023](#)), as illustrated by the reorganisation of trade and investment flows in favour of geopolitically close partners (friendshoring).

In 2019, the EU adopted a cooperation mechanism ([EU Regulation 2019/452](#)) for FDI screening. This mechanism, designed to strengthen the EU's strategic autonomy, has fostered the diffusion of ISMs in Europe. The Covid-19 pandemic ([Evenett, 2021](#)) and conflicts with Russia have also contributed to the adoption or strengthening of ISMs, particularly in Central Europe ([Bauerle and Meunier, 2023](#)).

**Chart 2: The rise in investment screening mechanisms in advanced economies**



*Note: while some economies have had ISMs for a long time (red boxes), their adoption is more recent in the EU, where some only adopted them few years ago (white boxes).*

Source: [PRISM](#) ©.

**FDI screening mechanisms vary across countries, including within the EU**

With no specific data available, it is difficult to assess the effect of FDI screening on transactions and, more generally, on the competitiveness and attractiveness of advanced economies. [Bencivelli et al](#) (2023) constructed a database documenting the heterogeneity of national legislation and developed an indicator measuring the degree of restrictiveness of these different mechanisms.

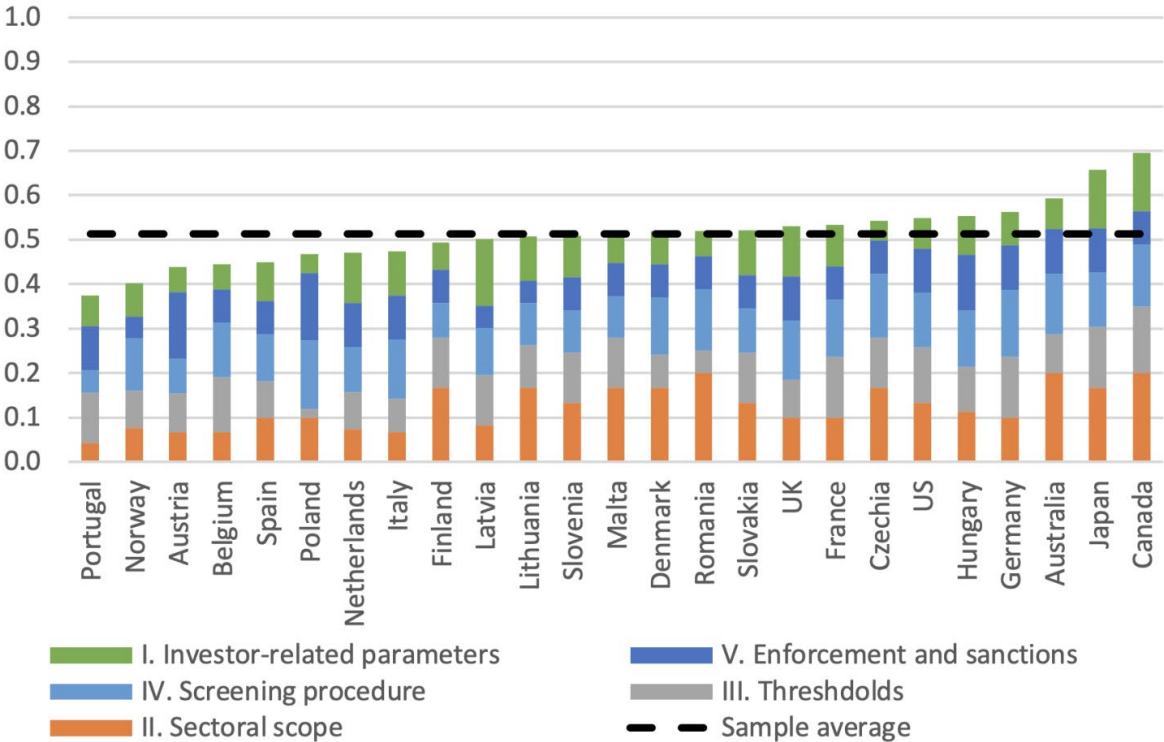
The indicator ranges from 0 (relatively open ISMs) to 1 (relatively restrictive) and covers five areas:

- the nationality and characteristics of the investors covered by the ISM;
- the sectors and type of transactions covered;
- thresholds (amount of transactions, acquisitions, etc.) triggering a screening process;
- screening procedure (maximum length of review process, investor disclosure obligations, etc.);
- enforcement powers and sanctions of the authorities.

The indicator suggests that the strictest ISMs are in Japan, Australia and Canada (Chart 3). In all three countries, investment screening covers a large number of activities deemed sensitive, and is reinforced for investment projects undertaken by public companies. Moreover, screening covers the acquisition of existing assets (brownfield) as well as investment in new facilities (greenfield). The authorities also have extensive investigation powers. In Japan and Canada, the thresholds for screening foreign investment are also relatively low.

This indicator assesses the pace of legislative convergence within the European Union. By defining the factors to be taken into account - such as the sectors targeted by foreign investors (critical infrastructure and technologies, media, etc.) and any links between the investor and the government of a third country - the European mechanism encourages the coordination, and even convergence, of national ISMs. Chart 1 shows that these ISMs are however heterogeneous. Differences in scope and the absence of ISMs in some Member States undermine the effectiveness of this mechanism ([OECD, 2022](#)), which will be assessed by the European Commission before the end of 2023.

Chart 3: Heterogeneity of ISMs in advanced economies



Note: The indicator ranges from 0 (relatively open ISMs) to 1 (relatively restrictive) and covers five equally-weighted areas. Each area includes several sub-components.

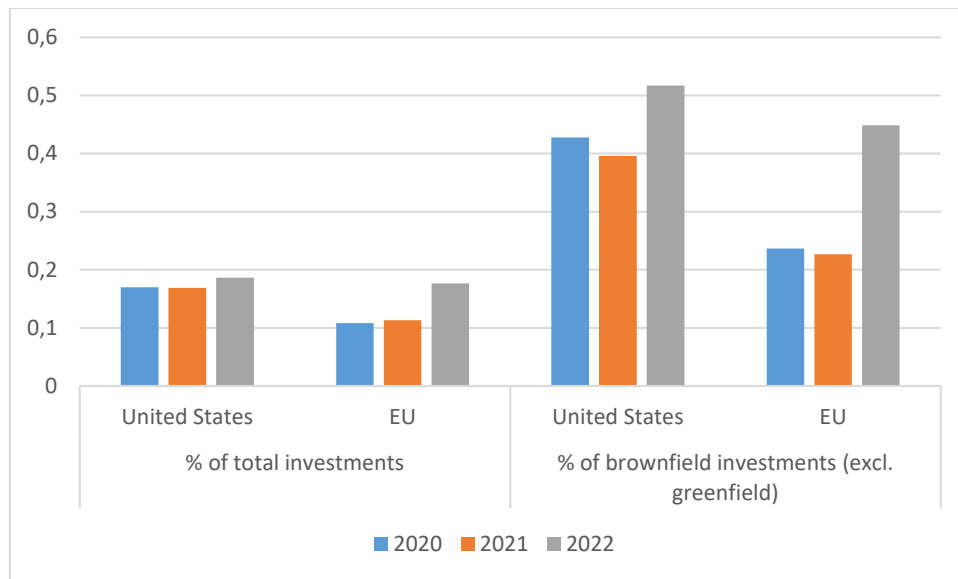
Source: Bencivelli et al., 2023.

[Bencivelli et al.](#) (2023) show that FDI screening in the interests of national security coexists with otherwise open investment regimes. Some of the strictest countries, such as Australia and Canada, attract significant FDI inflows. Furthermore, investor surveys ([Kearney, EY](#)) show that the recent strengthening of ISMs has not changed investors' perceptions regarding the most attractive destinations.

**ISMs strike a balance between opening up to FDI and protecting national interests**

A significant share of transactions are subject to FDI screening (Chart 4). For example, transactions screened in the United States accounted for 19% of inward FDI in 2022. Similarly, 18% of FDI from non-EU countries was screened under the European Cooperation Mechanism in 2022. This share exceeds 45% for brownfield investments alone, as greenfield investments are excluded from the scope of most ISMs.

**Chart 4: Share of screened inward FDI in the EU and the United States**



*Note: in 2022, transactions screened in the United States and the EU accounted for almost 20% of inward FDI, and more than 45% for brownfield investments alone.*

*Source: European Commission, CFIUS, authors' calculations.*

The increasing use of ISMs in the EU has contributed to the growth in the number of transactions screened in 2022. However, in both the United States and the EU, few transactions are blocked (1% in the EU, no transactions in the United States in 2022), which suggests that ISMs strike a balance between opening up to FDI and protecting national interests. The low percentage of transactions blocked could also reflect the deterrent effect of ISMs.

Information and communication technologies and the manufacturing sector account for the bulk of transactions screened or blocked, which is consistent with the scope of MFIs. These sectors include technology (artificial intelligence, robotics, etc.), critical infrastructure (communications, media, data processing and storage) and defence.

The geographical origin of the most screened investors is related to the weight of each nationality in FDI flows (the share of US investments in investment flows to the EU, and vice versa). However, in the United States as in Europe, some investments, particularly from China and Russia, are over-represented in the transactions that are screened and blocked. This over-representation reflects the predominance of Chinese investors controlled by state authorities and subject to particularly close monitoring in most ISMs.

The trend towards stricter FDI screening mechanisms continues apace. In the United States, the Biden administration announced in summer 2023 the creation of a screening mechanism for outward FDI, designed to limit the risk of technology transfers with potential military applications. The EU has affirmed its commitment to strengthening its economic security and analysing the risks posed by outward investments in its [European Economic Security Strategy](#) (June 2023).