

Addressing risks to the EU's economic security

Recent policy actions under the OSA agenda

Violaine Faubert – Banque de France*

8 April 2024

*The views expressed do not necessarily reflect those of the Banque de France.



Openness until recently regarded as a strength of the EU could turn into a **vulnerability** amplifying the transmission of **geopolitical shocks**

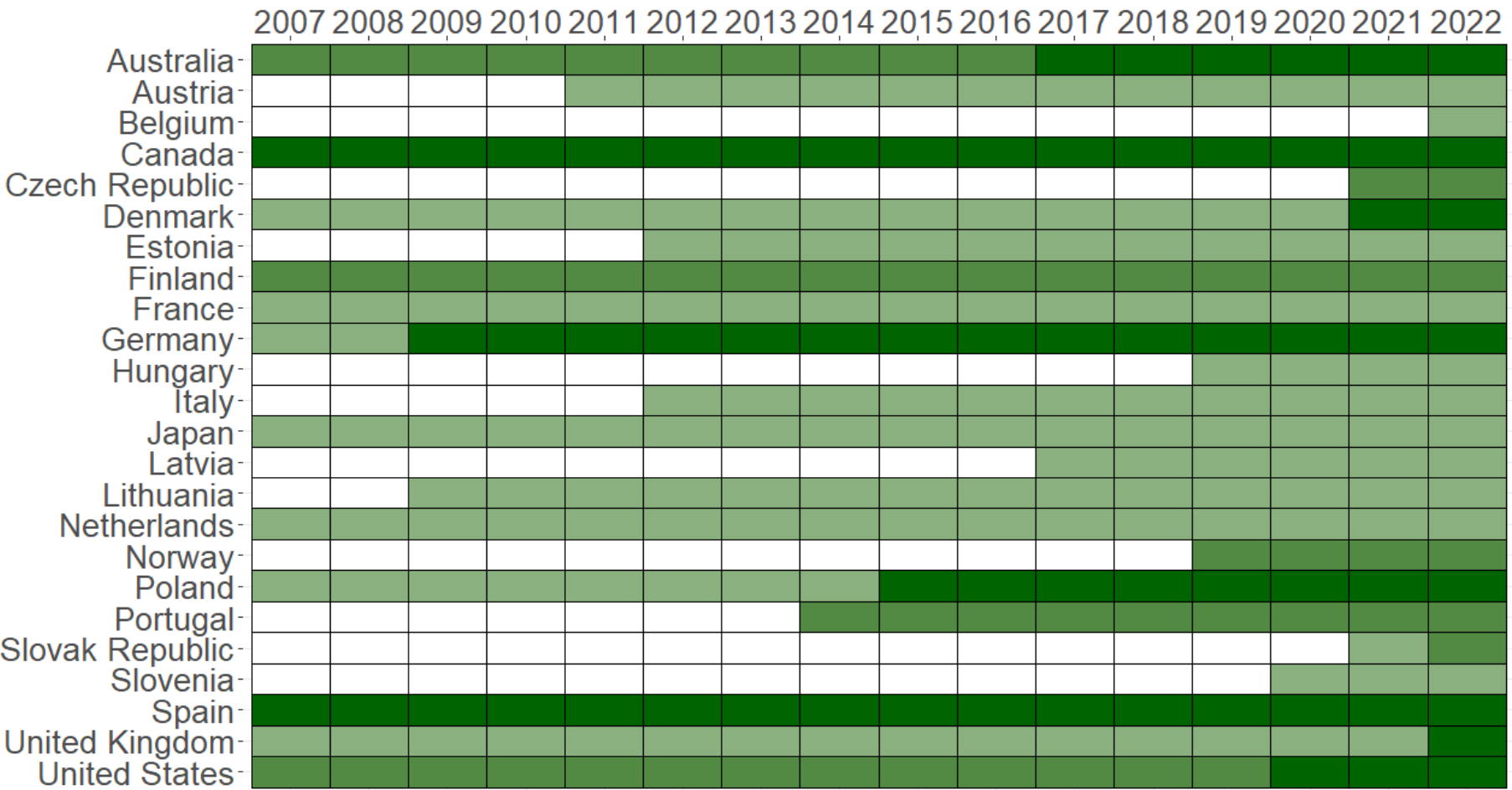
The EU has identified 4 risks to its economic security (June 2023):

- resilience of supply chains;
- disruptions of critical infrastructure;
- technology leakage;
- economic coercion

OSA policies to address economic vulnerabilities arising from geopolitics, while preserving economic openness:

- ⇒ **resilience** of supply chains: **Critical Raw Materials Act**
- ⇒ respond to **geopolitical threats**: **FDI screening** regulation

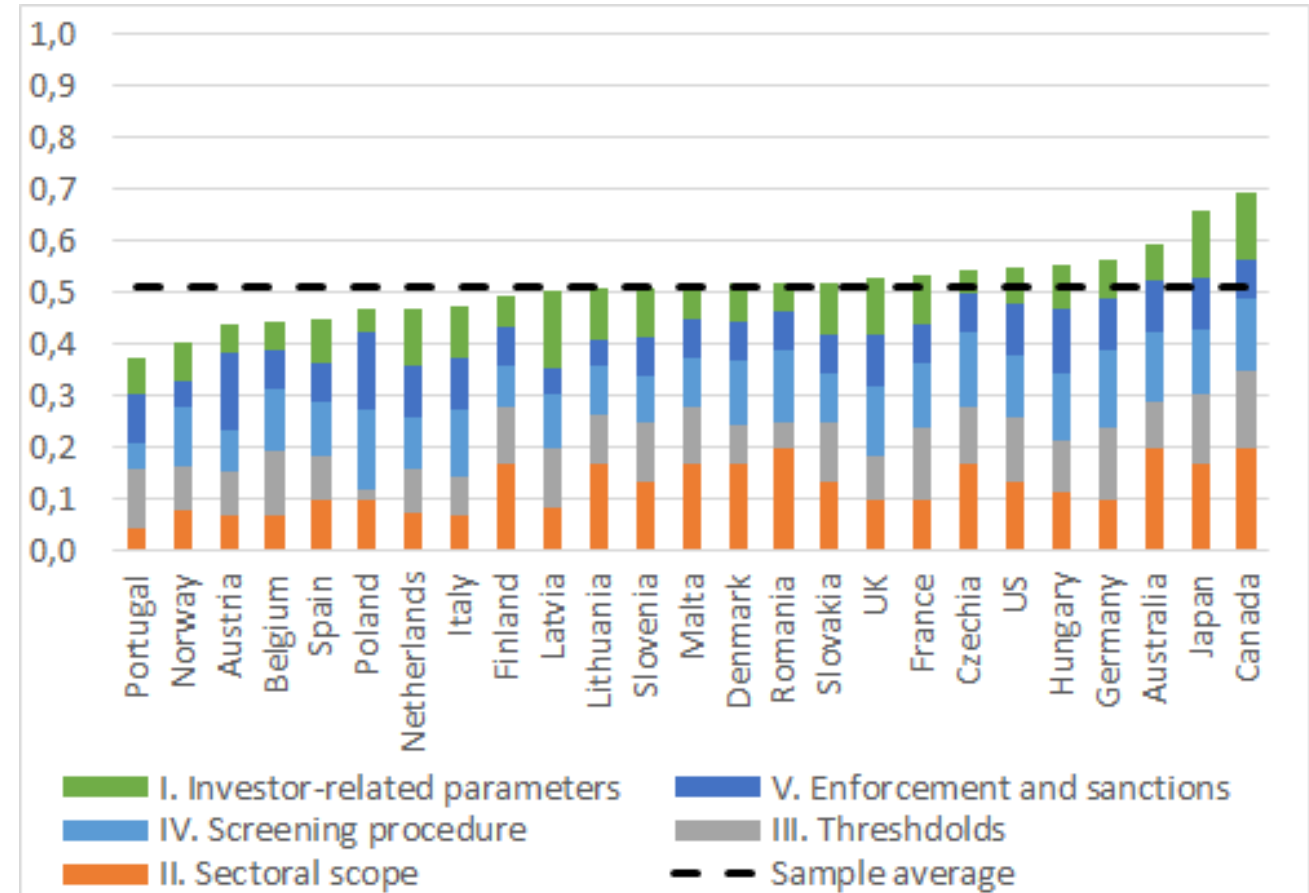
AFTER THE END OF INNOCENCE, THE AGE OF FDI SCREENING



Note: most countries that did not have an ISM (white) have adopted such mechanism (green). A number of countries have shifted from sectoral mechanisms (where the government has the authority to review a list of sectors, light green) to a cross-sectoral (green) or mixed mechanism (dark green), where the government can review investments in any sector and subject a specific list of sectors to stricter review requirements, Source: [Bencivelli et al. \(2023\)](#), based on PRISM (Meunier and Bauerle Danzman)

THE RISE OF ISM, THE FALL OF ATTRACTIVENESS?

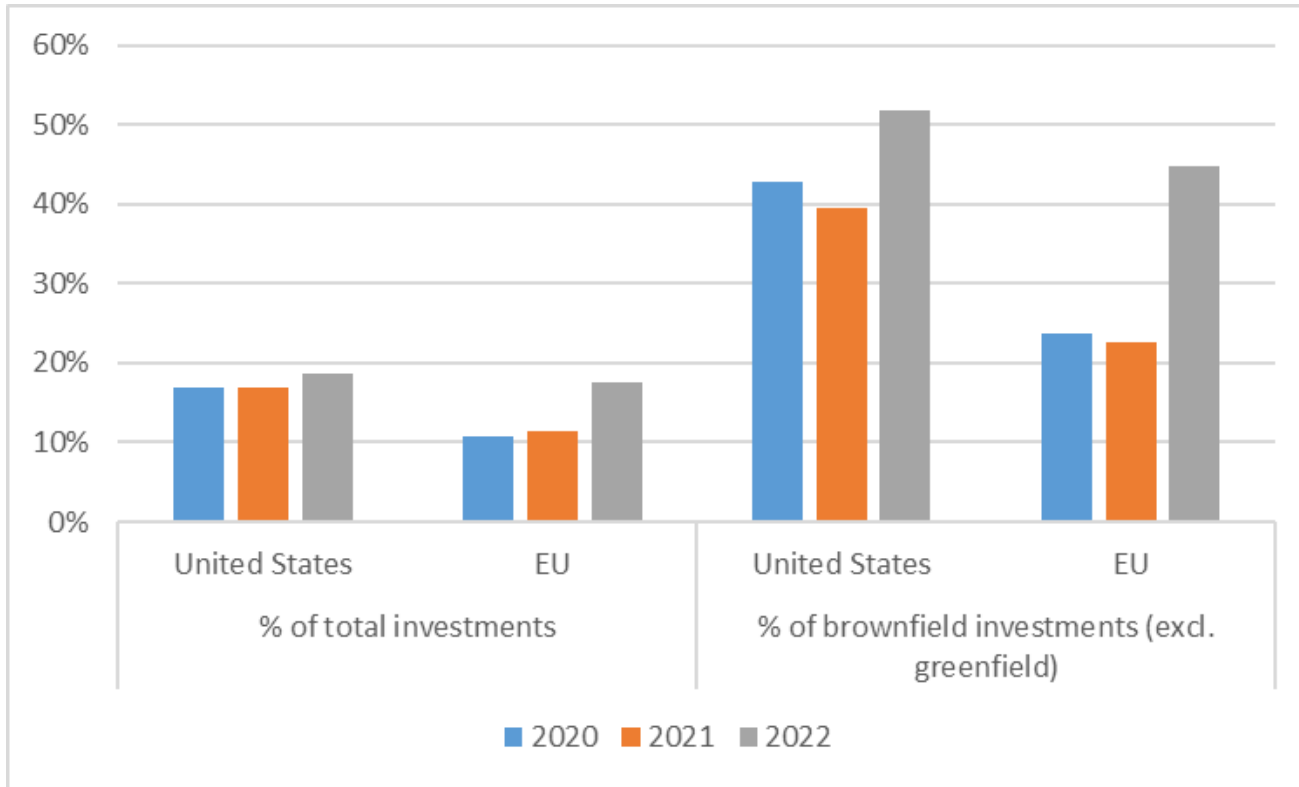
- EU has moved in the same direction as other economies: 80% of the 61 economies that participate in the Freedom of Investment Roundtables screen FDI (20% in 2012, OECD)
- Most restrictive ISM laws: extra EU
- Recent tightening of ISMs has not coincided with investors' reappraisal of the most attractive destinations (eg. Kearney's FDI Confidence Index)



The index ranges from 0 (relatively less restrictive) to 1 (relatively restrictive).

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

THE COST OF ECONOMIC SECURITY



- Significant share of transactions subject to screening as a share of all inward investment (12% FI, 20% FR in 2022)
- Majority of transactions subject to scrutiny authorized without conditions (98% DE, 92% IT, 86% ES; 47% FR in 2022)
- Few transactions blocked (1-2%)
- No evidence of a “chilling effect”... but anecdotal evidence on the cost of screening (eg: Photonis)

[Bencivelli et al. \(2023\)](#), based on CFIUS, US BEA and EC

BLIND SPOTS

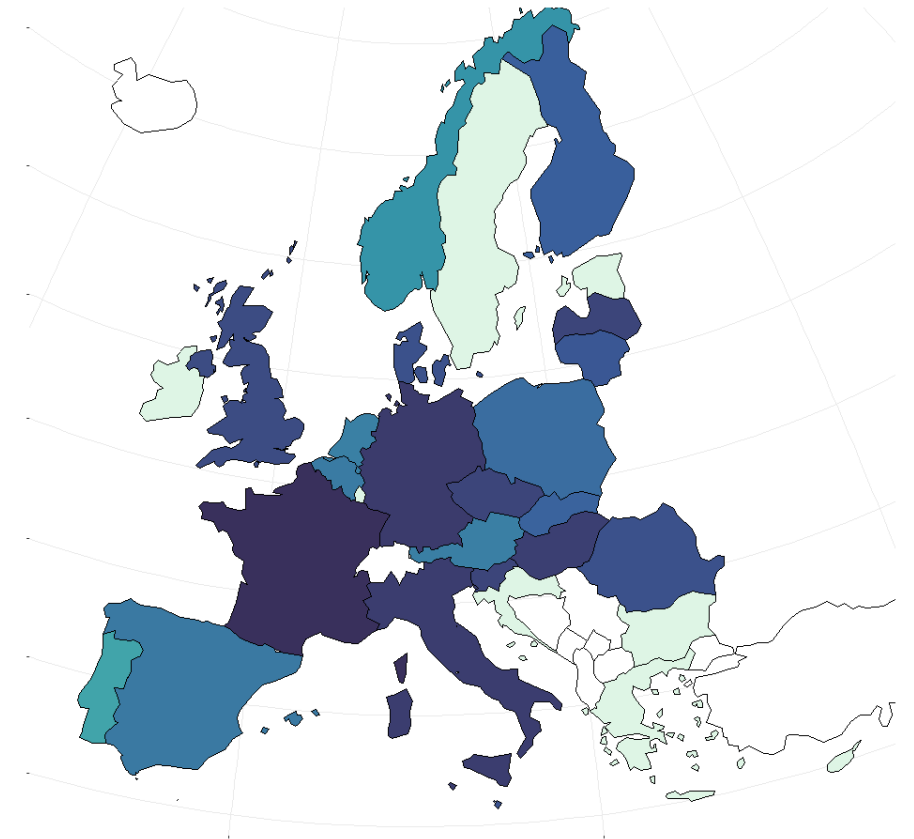
Potentially risky transactions can go unnoticed

Assessing the EU regulation:

- Momentum: 22 (24 soon with IE and BG) MS have an ISM, vs 13 in 2017
- Blind spots:
 - Lack of ISM: 23% of the foreign acquisitions were in MS lacking an ISM (2019-23)
 - Heterogeneity of national ISM
 - Room for improvement: accountability, coverage of intra-EU transactions...

Economic security strategy (2024):

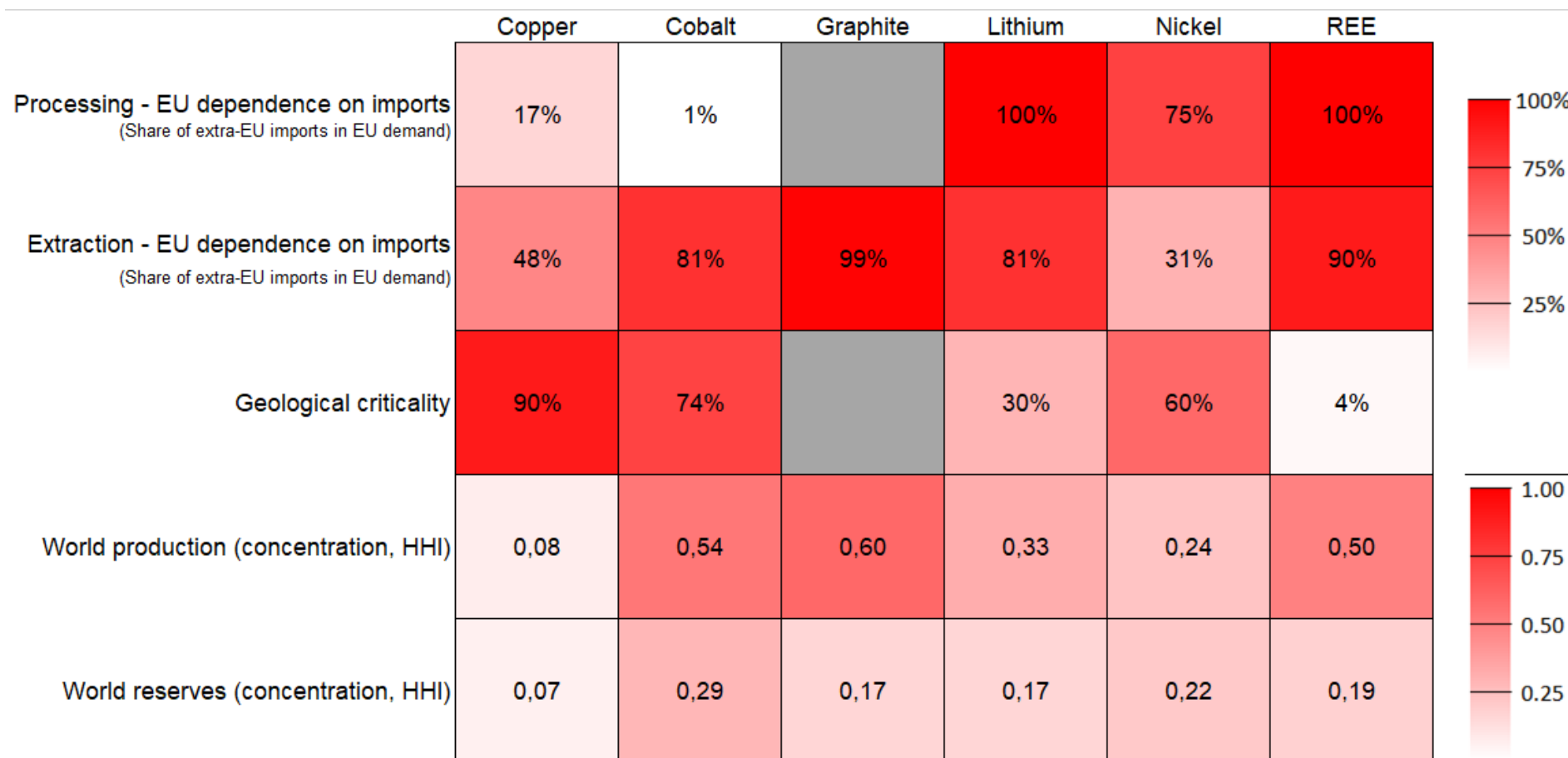
- Proposal for a new regulation on FDI screening
- Consultation: identifying potential risks stemming from **outbound** investments



Dark (light) blue: relatively more (less) restrictive ISM. Green: legislative process expected to result in the adoption of a new mechanism.

[Bencivelli et al. \(2023\)](#)

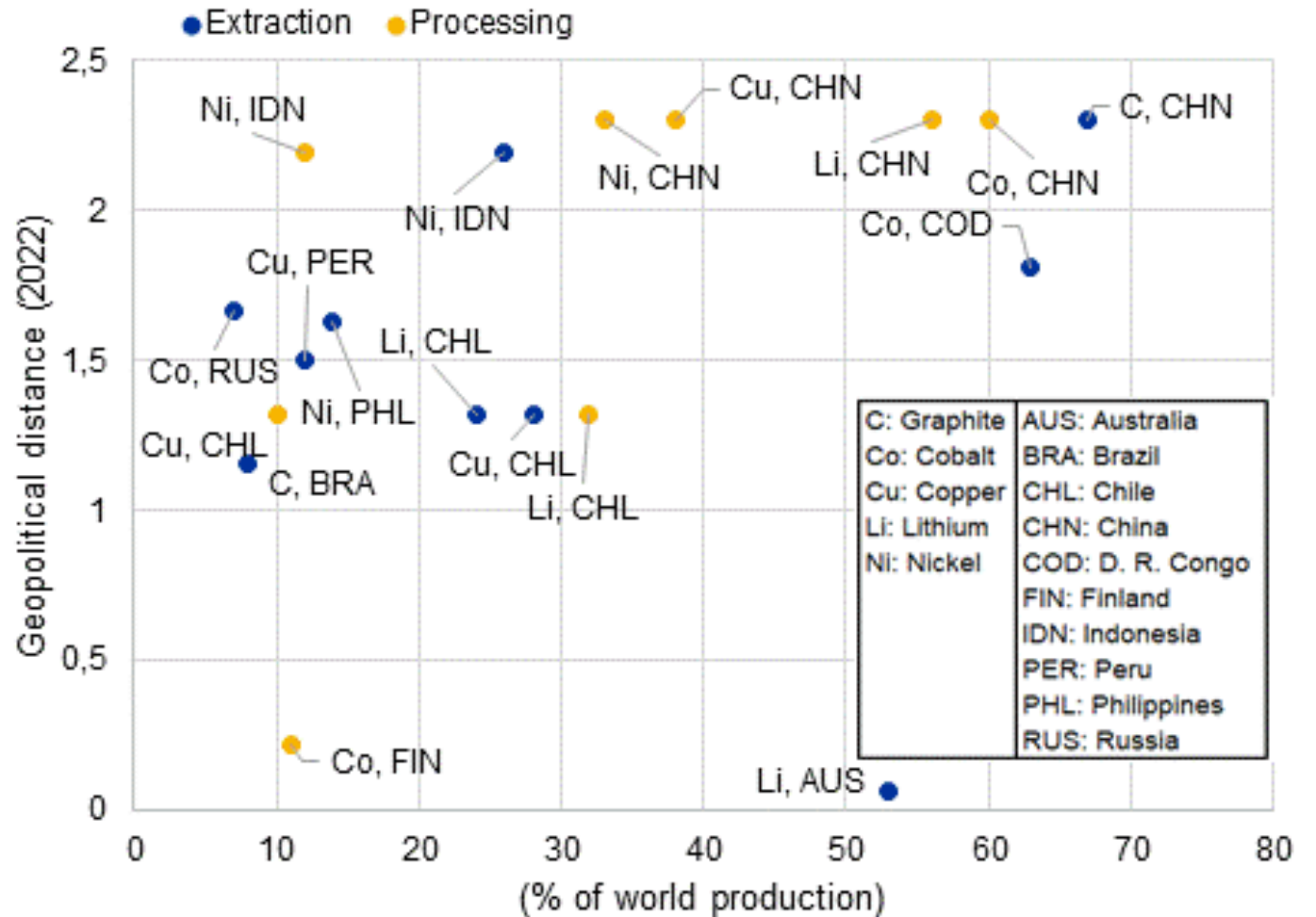
CRITICAL RAW MATERIALS: the EU relies on imports from a limited number of countries



Note: the darker the red, the more concentrated the supply, the greater the EU's dependence on imports and the greater the geological criticality (missing data in grey). Source: [Faubert et al. \(2023\)](#), based on USGS, EC, IFPN

CRM- VULNERABILITIES OF THE EU

- Mining and processing concentrated in countries that are not politically aligned with the EU:
 - cobalt in DRC
 - REE in China,
 - nickel in Indonesia...
- Central role of China at the processing stage (REE, cobalt, lithium, nickel, copper)
- EU vulnerable to supply disruptions and geopolitical risks



Source: [Faubert et al. \(2023\)](#), based on EC and Bailey (2017)

THE CRM ACT SETS OUT AMBITIOUS TARGETS

- **Extraction** (10% of EU annual consumption)
 - Limited exploration in the EU : 2% of the world's mineral exploration investment ([Hache et Normand, 2024](#))
 - Revitalizing the European mining industry will require substantial funding... but mining projects are not included in the European taxonomy of low-carbon investments and do benefit from a dedicated budget
 - Short time horizon (2030): 7 (lithium) to 17 years (copper) between exploration and production
- **Refining** (40%)
- **Recycling** (25%)
 - potentially recyclable products are integrated into long-life consumer goods
 - not all recycling technologies are profitable
 - rapid developments in battery chemistry make investment in these technologies risky
- **Diversifying**: no more than 65% of the EU's annual consumption from a single third country
 - currently the case for half of all strategic raw materials (Grohol and Veeh, 2023)
 - finding alternative suppliers is a long-term undertaking: multiplication of bilateral strategic partnerships
 - difficulty of measuring the achievement of such a target on an EU-wide scale

CAPITAL IN THE XXIth CENTURY: Who controls the capital of firms involved in CRM extraction?

Other major economies depend on imports

- eg. China heavily reliant on African exporters
- Long-term strategies to secure CRM

Who controls the capital of the top mining companies ?

- Dominant role of China (REE, lithium, cobalt)

	China	United States	EU	UK
Rare-earth elements	65%	19%	1%	4%
Nickel	13%	20%	21%	7%
Lithium	54%	23%	3%	4%
Copper	28%	26%	6%	8%
Cobalt	29%	14%	1%	6%

Source: [Faubert et al. \(2023\)](#), based on Refinitiv and companies annual reports

OSA policies imply trade-offs (economic security vs economic efficiency), and need to be appropriately calibrated ([Ioannou et al., 2023](#))

- Resilience of supply chains: reorienting trade towards reliable partners may imply higher costs;
- Managing geopolitical threats: FDI screening may be necessary to protect strategic sectors but may also reduce the availability (“chilling effect”) and efficiency of capital allocation (transactions delayed, impact on price), especially if uncoordinated within the EU.