Where the Silk and Amber Roads Meet

China in Central and Eastern Europe

By Michal Romanowski

Central and Eastern Europe are playing an increasingly important role in China’s global ambitions, not least because they are geographically located along the New Silk Road that Beijing seeks to build through massive investments in roads, railways and ports.

But China’s embrace of the region is running up against a host of concerns in the countries involved and gradually drawing Beijing and the European Union into a contest for influence, writes Michal Romanowski.

WHAT DO A steel mill in Poland, a brewery in the Czech Republic, a sea port in Bulgaria and a high-speed railway in Serbia have in common? It seems like a testing question in an international affairs quiz. But for China followers, the answer is simple. All these businesses and projects are either owned or operated by Chinese companies.

Over the last decade, Beijing has boosted its economic and political presence in Central and Eastern Europe (CEE), symbolically re-connecting two ancient trade routes linking Europe and Asia — the Silk Road and the Amber Road that once served as a bridge between the Roman Empire at the Mediterranean Sea and the south coast of the Baltic basin. Today, China sees Central and Eastern Europe as a sub-region at the crossroads between the European Union and Eurasia. The so-called 16+1 format launched in 2012 that brings together 16 CEE countries and Beijing is an instrument in China’s global outreach strategy. China’s Belt and Road Initiative (BRI) — the modern incarnation of the Silk Road — has given the CEE-China platform regional importance.

While having an economic presence in Central and Eastern Europe, China plays multiple roles at the same time. The sixth meeting of the heads of state of the CEE countries and China, held in November in Hungary, offers a pretext for examining the different roles Beijing plays in the region.

ROLE NO. 1: CONNECTOR

In the past, the Great Wall of China symbolized the Middle Kingdom’s isolationism. The fortifications were built to protect the Chinese state against nomadic groups from the Eurasian steppe. In the 21st century, however, Beijing has emerged as a major proponent of globalization and international connectivity without boundaries. The processes initiated by Deng Xiaoping’s reforms of the late 1970s have positioned China as the world’s new economic center of power.

This narrative attracts many in the CEE region who would like their countries not only to be more deeply embedded into the global market, but also to cultivate bilateral relations with Asia’s main actor. The BRI is an opportunity for Central and Eastern Europe to make its mark on history and simultaneously benefit from Chinese capital and investment.

The BRI aims to foster economic development, investment and cultural exchanges across Eurasia and is an umbrella to facilitate the rise of China’s political profile. But it also has a practical economic dimension. In the period 2014-2016, trade between the countries along the new Silk Road exceeded US$3 trillion and Chinese direct investment surpassed US$50 billion. Even the most skeptical among the elites of Central and Eastern Europe are tempted by a vision of their country’s economic dimension. In the period 2014-2016, trade between the countries along the new Silk Road exceeded US$3 trillion and Chinese direct investment surpassed US$50 billion. Even the most skeptical among the elites of Central and Eastern Europe are tempted by a vision of their country’s increased attention Brussels pays to Chinese operations in the region.

Beijing’s financial firepower — including tens of billions of dollars in credit lines, the engagement of mammoth state-owned enterprises, and direct investments through capital infusions and acquisitions — is unprecedented in its scale. But it should be remembered that China has grown into a global connector not only out of goodwill, but because doing so is in line with its national interests. The same pragmatic approach should be adopted by the CEE region and more broadly by the European Union.

ROLE NO. 2: SHAPER

A brief look at the 16+1 initiative is enough to identify the brains behind this project. China took a proactive approach to gathering the countries of the region together, promising mutual economic gains. Today, the format has developed into a loosely administered club with regular high-level meetings, national co-ordinators and a joint secretariat.

As the CEE-China platform enters its sixth year, there is more understanding on both sides when it comes to the context of co-operation as well as the results and future prospects. However, there is still a tendency in China to approach the region,
which is an exceptionally heterogeneous bloc, as one. The initial optimism has now been replaced in the CEE with a more cautious stance.

China has been modelling the collaboration and presents it as a success — and in some respects Beijing has achieved its goals. The country’s standing in the region has improved, and several investment projects have taken off. Trade with Central and Eastern Europe as well as Chinese direct investments are also expanding. In this respect, the picture should be more nuanced, because both were already on the rise before the establishment of the 16+1 and the launch of the BRI. In addition, this should be seen in perspective, given that over 50 percent of Chinese investments in Europe flow to the big four EU countries: Germany, France, Italy and the UK.

In retrospect, China has missed the opportunity to establish a common 16+1 denominator — a goal around which all the countries would unite. China-sponsored big-ticket infrastructure investments have proven to be insufficient to keep the momentum for CEE-Beijing co-operation going. As a result, opinions in Central and Eastern Europe on China and its engagement in the region differ to a great extent.

Most of the governments seem to have a neutral stance toward the Chinese leadership, attaching minor relevance to the proposed BRI projects in their countries. Hungary and Serbia, being the most receptive to capital arriving from Beijing, could be counted among the greatest China enthusiasts. The Czech Republic is an interesting case in this regard. President Milos Zeman is exceptionally vocal about the positive role China could play in the region. He has even appointed a vocal delegate, but also by public protesters accusing Beijing of human rights violations in Tibet.

The Chinese vision of co-operation with the CEE region is pragmatic, but so far its implementation has been weak. Promises of massive investments without the needed follow-up and empty declarations that are not translated into reality seem to have caused increasing fatigue. Some voices coming from Beijing are additionally complicating the political picture. A chairman of the foreign affairs committe of the Chinese parliament said that the first country in Central and Eastern Europe to create the most friendly business environment for China will likely become a CEE Silk Road hub. This promise of win-win co-operation model, transformed into fierce competition among the CEE countries, will distort the original idea of international co-operation benefiting all.

**ROLE NO.3: INVESTOR**

Another face of China in Central and Eastern Europe is that of an investor. Europe as a whole, including the CEE region, has experienced considerable growth in Chinese foreign direct investment (FDI). In 2003, Chinese FDI amounted to US$400 million, whereas in 2016, it reached record levels of over US$40 billion.

Looking at the issue through the prism of the CEE, the region receives approximately 10 percent of China’s total investment in Europe. In contrast, roughly 90 percent of assets arriving into Central and Eastern Europe hail from the EU and the US. While China does not appear to view the region as a main investment destination, the CEE is reciprocating that concept by looking to the West, not the East, for funds.

Nevertheless, Beijing is present and investing millions in infrastructure projects, industry, services and the entertainment sectors. The CEE area does not, however, receive equal attention from the Chinese government and Chinese enterprises. Until 2015, Hungary attracted over three-quarters of all CEE investments by Beijing. Today, the Visegrad Group, encompassing Hungary, Poland, Slovakia, and the Czech Republic, accounts for half of CEE-China trade turnover as well as the majority of Beijing’s FDI.

In recent years, Chinese investments in the region have followed a similar pattern. Beijing concentrates on mergers and strategic acquisitions in industry and services. Greenfield ventures are not part of the Chinese FDI blueprint. In order to receive support from Beijing, projects should fully or substantially be executed by Chinese companies with the local government providing guarantees that loans will be repaid. This approach promotes not only Chinese capital, but also its technology and workers.

In this financial model, China increasingly creates the impression that it is a lender not an investor. Consequently, Beijing has various credit entities (apart from state banks) at its disposal to stimulate regional investments. The China-CEE Investment Co-operation Fund, with US$1 billion, is a private equity fund that will focus on acquisitions. A second fund — run by the Sino-CEEF Holding Company with capital over US$10 billion — is expected to focus on developing infrastructure, high-tech manufacturing and mass-consumption industries.

Easy access to Chinese capital could be particularly risky for smaller 16+1 players, where uncontrolled growth of debt could pose threats to the fiscal stability of their economies. For instance, a 2014 loan from China for a highway project saw Montenegro’s public debt increase by 23 percent.

One of the most highlighted investments by China in the CEE region is the high-speed railway between Serbia and Hungary. The Export-Import Bank of China is providing 85 percent of the funds for the project. With a designed maximum speed of 200 kilometers per hour, it expects to reduce the travel time between Bel-
It is believed that Chinese infrastructure projects in Central and Eastern Europe might come with a political price attached. Some countries seeking not only investments, but also alternative political affiliations, are already willing to pay that price. The EU probe in Hungary is looking at whether the China-Hungary deal on the high-speed railway is in accordance with EU law on public tenders in infrastructure.

ROLE NO. 4: CHALLENGER

This phenomenon reveals another face of Beijing in the CEE region. As the Chinese economic footprint in Europe enlarges, so does the interest the European Union pays to China’s activities. The Asian superpower — from the perspective of Paris, Brussels, or Berlin — is increasingly seen as an economic and political challenger in Europe and globally.

After a series of high-profile Chinese acquisitions in 2016-2017, including the Swiss chemical company Syngenta and the German robotics group Kuka AG, officials in Europe were in a state of near panic. French President Emmanuel Macron said that Europe needs to curb foreign takeovers in strategic industries and that it should not be naïve about global trade.

In September 2017, European Commission President Jean-Claude Juncker said that all foreign, state-owned companies that intend to purchase a high technology firm or part of critical EU infrastructure should do so in a transparent and scrutinized fashion. He proposed a screening framework to avoid foreign takeovers in sensitive sectors in the future. Germany has already tightened its rules on corporate acquisitions and another 11 EU countries are exploring changes to their national control regimes.

Not only Chinese investments across Western Europe, but also those in the CEE region are regarded by some as a threat to the European Union. German Foreign Minister Sigmar Gabriel said recently that if Europe does not succeed in developing a single strategy towards China, then China will successfully divide the continent. As an example, in 2016, Hungary and Greece — major recipients of Chinese capital — blocked a more firm EU Council declaration on Beijing’s operations in the South China Sea.

Brussels understands that in order to be most effective in its approach toward China, the EU must speak with one voice. In the same address, Minister Gabriel called on Beijing to follow a policy of “One Europe,” just as the EU follows the “One China” policy — a comment that was sharply criticized in Beijing.

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Currently, it seems that the EU’s development offer to the CEE region, including both the bloc’s members and aspiring countries, is still more attractive than the Chinese proposition. Brussels provides free-of-charge subsidies within its structural and cohesion funds, whereas Beijing grants conditional loans. The competition for influence between the EU and China in the region has more to do with relations between the two than with Central and Eastern Europe itself, which serves as only one of the catalysts for the dialogue.

The European Union and Chinese authorities share a vision of an open and balanced global governance system and promote stability and peace across the Eurasian supercontinent. In theory, both should work hand in hand. Yet, the devil is always in the details. The lack of mutual understanding on a broad range of policy issues (the South China Sea, access to the Chinese market, unfair competition, human rights) coupled with different business cultures and EU legal requirements impede progress in the bilateral relationship.

CONCLUSIONS

China has long kept its activities in Central and Eastern Europe low profile. Over the past five years, however, Beijing has both declared and demonstrated a political and economic commitment to the region.

Today, the major obstacle for the 16+1 format is the lack of willingness among its members to identify and articulate common interests and policies. As a result, one can observe 16+1+1 platforms, where bilateral ties with Beijing play the key role. In the long term, fundamental uncertainties regarding China’s intentions could complicate relations between Beijing and Europe as a whole. The CEE region is an arena where both sides might either entrench themselves in their positions or seek an open dialogue.

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