# THE CHINESE INFLUENCE IN CENTRAL EASTERN EUROPE DURING THE GLOBAL ECONOMIC CRISIS

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### *Chinese investments in Central Eastern Europe: some introductory features*

Statistics relative to the economic relationship between Central Eastern Europe and China suffer of inhomogeneity of data. First of all, statistics on investments are strongly heterogeneous. European and Chinese data are considerably different. Data from the Chinese side, and in particular that from the Ministry of Commerce (MOFCOM) suffer of several limitations [Korniyenko and Sakatsume, 2009]:

- MOFCOM data include only the investments approved and registered by the Ministry. The registered investments not necessarily correspond with the actual amount of outward investments. As a matter of fact, the investments may defer in many years after the registration time and tiny investments do not need any registration. Furthermore, MOFCOM data consider re-invested earnings form outward investments [Apoteker, 2012; Apoteker and Barthélémy, 2013].
- MOFCOM data do not consider Chinese outward investments originating from Macao, Hong Kong and such offshore fiscal heavens as the Virgin and Cayman Islands; the flow of funds towards the fiscal heavens, indeed, is quite relevant but it appears strongly unlikely that funds that stay do not move elsewhere [Hanemann, Rosen and Richard, 2012; Godement, Parello-Plesner and Richard, 2011; Banca Naţională a României, 2006; Nicolas and Thomsen, 2008].
- MOFCOM data do not usually consider financial and bank investments.
- Moreover, data collecting methodologies suffered of many variations and mutations during the years.

Because the above mentioned elements, some scholars prefer the European statistics or data coming from international economic organizations. Some [Hanemann and Rosen, cit.] have elaborated new economic index in order to analyze the Chinese investments outward. This study, however, will try to compare both European and Chinese data, aiming to sketch a broad picture of the Chinese foreign direct investments in Europe.

Broadly speaking, scholars agree on some features of the Chinese investments outward. Indeed, the Chinese FDIs outward aim [Korniyenko and Sakatsume, cit.]:

- to explore new markets;
- to look for specialized low cost workforce still missing in China [Milelli, Hay and Shi Yunnan, 2009];
- to search for raw materials;
- to buy strategic assets, international brands, new technologies;
- to diversify the companies' own production and portfolio;
- to flow out capitals and reduce the international pressure on the renminbi appreciation;
- to reduce the high levels of savings;
- to gain from the low taxes and duties on the FDIs outward;
- to try to avoid anti-dumping rules, especially in Europe.

Even missing raw materials, Central Eastern Europe represents a potentially perfect scenario for the Chinese FDIs. In particular, the access of the CEE countries to the European Union may be a powerful pull factor for Chinese FDIs in order to avoid Brussels' anti-dumping rules [Filippov and Saebi, 2008].

Nevertheless, the Chinese FDIs are still a small segment of the total world investments. In 2007, the investments from China accounted just for a 1.1% of the world total [Nicolas, 2009]. Indeed, the huge growth rate of the Chinese FDIs outward bases on the low starting level. Moreover, Europe accounts just for a small share of the Chinese investments outward [Ebbers and Zhang, 2010; Zhang, Zhi and Van Den Bulcke, 2012].

In addition to the foreign direct investments outward, China is probably considering to buy shares of the European public debt. The real amount of such a shopping, however, is unclear as well as is probably not much relevant, but "*it is useful for China's public diplomacy to suggest it is a potential benefactor*" [Godement, Parello-Plesner and Richard, cit.].

Considering the structure of the Chinese investments in Europe, it is possible to note the focus on merger with and acquisition of European firms. Almost 80% of the Chinese FDIs in Europe are M&A. Chinese M&A focused prevalently on European firms in bad financial situation: selling the assets to the Chinese allows the European side to restructure the firm's financial organization and to access the Asian market. Beijing is looking also on joint ventures with European firms (20% share of Chinese FDIs in Europe) but less on greenfield investments (1%).

**The Chinese Influence in Central Eastern Europe: a link between economic and politics?**

Chinese investments in Europe have not always been successful. Indeed, Chinese FDIs in Europe must face some negative factors such as the bureaucracy, tiny access to funds, shortage of strong convertible value, lack of experience in investing abroad. With regard to the last factor, Central Eastern Europe may be the training gym for the Chinese Companies interested to invest in the European Union. These companies can acquire in the CEE countries the knowledge and experience necessary to access the more difficult and competitive markets of the older EU members [Ying Zhang and Filippov, 2009; Russell Hsiao and Czekaj, 2011]. Indeed, Table 2 shows the rise of the stock of non-financial Chinese FDI in Central Eastern Europe.

Not all that glitters, however, is gold. Table 3 shows that the Chinese FDIs in CEE countries are just a small fraction of the total Chinese investments in Europe. Moreover, the Chinese Deputy Foreign Minister, Fu Ying, noted that "*Chinese companies do face some difficulties in the European market. For one thing, they are not familiar with the political, legal and social environment in Europe and do not have adequate managerial expertise, therefore need help from local companies and legal protection. For another, some European media accuse them of ulterior motives. This dampens their investment enthusiasm. As a result, they would rather head elsewhere for opportunities, since the investment environment in Europe is not considered favorable*" [Dikov 2011]. The Bulgarian Deputy Prime Ministry for Economic Development, Daniela Bobeva, outlined that many of regulatory conditions in Europe are "*restrictive, almost forbidding for Chinese construction companies*" [Dikov, cit.].

As a matter of fact, Chinese companies face many difficulties investing in Europe and lose many international tenders. Here some examples: China Huadian Engineering, China National Electric Engineering, Minmetals Engineering Co. Ltd., Sinohydro tried to participate in a bid for the construction of a thermoelectric plant in the Tulcea region, Romania, but the Chinese companies have been rejected from the selection [Wall-Street.ro, 2012]. In 2009, the China Overseas Engineering Group (COVEC) won a public bid in Poland to build a highway segment but it has been a great failure, with the Chinese company forced to withdraw from Poland and a judicial controversy with the Polish Government [Cienski, 2011].

In the light of the above mentioned facts, it seems hard to note a link between the Chinese investments in Europe and hypothetical political shadow aims. Perhaps there are some economic inconveniences: an example is the phenomenon of reverse spillover. Outward investments usually create a spillover of technology and knowledge to benefit the destination countries' industries. Japanese FDIs in Czech Republic and Poland are good examples of this dynamics. Chinese investments in Europe, however, point mostly to accede the European technology, causing the so called reverse spillover phenomenon [Meunier, Burgoon, Jacoby, 2014].

Nevertheless, European members and common institutions continue to be highly suspicious of China's real aims and fear that Beijing could use the economic penetration for political goals [Jiang Shixue, 2013]. The nature of the Chinese State-Owned company, as well as the strong connections between some huge private companies, such as Huawei, with the Party, feeds that fears.

Actually, the current economic crisis affecting Europe appears to be changing the rules of the game.

**The role of the economic crisis in the China-CEE connection**

As a matter of fact, CEE countries, Poland excluded, are deeply affected by the economic crisis. Furthermore, the EU institutions seem to be inefficient in resolving the crisis. With a tide wave or euro-skepticism spreading all over Europe, CEE countries are looking to East in order to find a key solution to recover from the crisis. Countries such as Hungary, Poland and Romania appear to be the most confident in fastening ties with China.

Hungary is probably the most euro-skeptic country in the European Union. Despite some anti-Chinese words in the past, since 2010, the Hungarian Prime Minister, Victor Orbán, has been making huge efforts in fastening the relationship with Beijing. Orbán announced the rise of a "*new alliance of major significance with the People's Republic of China*" [Andromidas, 2013]. The former Chinese Premier, Wen Jiabao, visited Hungary in 2011. In February 2014, Orbán went to Beijing. China and Hungary signed several agreements on the infrastructure sector and Chinese investments raised fasten in the last years [Kałan, 2013; Bodnár, 2014; Vitéz, 2014]. Today, almost 3.000 firms with Chinese capital are active in Hungary but most of them relate to migrants arrived in the Central Eastern European country at the beginning of '90s. The main important Chinese brand in Hungary is Huawei. The Chinese telecommunication giant opened a logistic and distribution center in Budapest. The center is the biggest ever opened by Huawei outside China. Moreover, Yantai Wanhua Polyurethanes Co. Ltd. recently acquired the Hungarian chemical firm Borsodchem Zrt., an investment worth $ 1.9 billion [Chinaroom.eu, 2014; Meunier, 2013].

Perhaps, Hungary is the CEE country most interested in China but Beijing is probably more interested in a different CEE country, Poland. That is because Polish economy is well performing despite the European overall crisis. Indeed, the huge amount of Chinese investments towards Hungary registered in 2010 is especially due to the Borsodchem acquisition, something really exceptional for Chinese FDIs in Central Eastern Europe, but the best perspectives for the future of Chinese FDIs in CEE are in Poland, where the telecommunication giant Lenovo established a productive plant in 2008. The Bank of China and the Industrial and Commercial Bank of China recently opened branches in Warsaw [Deloitte, 2012]. In 2013, Guangxi Liugong Machinery Co. Ltd. bought a branch of the Polish Huta Stalowa Wola. Some Chinese state-owned companies are also interested in the Polish energy sector [Ding Qingfeng, cit.].

Romania follows Hungary and Poland as the third CEE country most interested in Chinese investments but ranks just fourth as a destination of Beijing's FDIs in Central Eastern Europe. Romania boasts decades of good relations with China during the Cold War and at the beginning of the '90s Bucharest was the eighth destination for Chinese investments. The value of these investments, however, was extremely low. Moreover, the process of economic modernization has been slower in Romania than in other CEE countries. As a consequence, despite the continuous but unfruitful efforts exercised by the Romanian authorities, Chinese investors seem to prefer Hungary and Poland. According to MOFCOM data, therefore, in 2003 Romania accounted to be the fifth European destination for Chinese non-financial FDIs, but its share quickly declined to be irrelevant in 2010.

Considering that the Balkan country does not offer attractive companies for merger and acquisition, Romanian authorities are focusing on the infrastructure and energy sector. Ponta's government is showing a deep involvement in attracting Chinese investments. During the summer of 2013, the Romanian Prime minister went to Beijing and expressed the auspice that "*Romania can be the best gateway to Europe, both literally - through the port of Constanta - and symbolically, a part of the investment might enter Romania too*" [Actmedia.eu, 2013]. From their side, Chinese firms show interest in various infrastructure and energy projects proposed by Romanians but are worried of the local bad legislation environment and the level of corruption in the Balkan country. The China-CEE forum held in Bucharest at the end of November 2013 has pushed for acceleration in the negotiations. The forum held in Bucharest has been the third edition of the meeting, after past editions held in Budapest and Warsaw. The Chinese Premier, Li Keqiang praised Romania's commitment with the organization of the forum as well as predicted that "*Romania will become Europe's tiger and if all tigers join and communicate a huge market will develop*" [Actmedia.eu, 2013]. China and Romania has signed several economic agreements on that occasion, involving the implementation of some railway infrastructure projects, of a Technology Park, of the Romanian export of meat and livestock to China. Various Chinese companies, such as the Sinohydro Corporation, the China Huadian Corporation, the China National Electric Engineering, the Mingyang Wind Power Group, the BAOTA Petrochemical Group and the JUNLUN Petroleum Corporation, signed agreements and memoranda with Romanian firms in the energy sector [Dinca, 2013; Ionascu, 2013]. China also signed a very important agreement with Hungary and Serbia to build an international railway [Xinhua, 2013].

The main outcome of the forum has been the elaboration of the so-called "Bucharest Guidelines" to address the bilateral relationship between China and CEE countries. According to the document, China and the CEE countries will regularly promote the organization of economic forums and summit meetings. It encourages small and medium companies to cooperate, to develop agriculture cooperation, and it also calls financial institutions for collaboration. Strengthening cooperation in investments and infrastructure, above all on railway networks, will be a further main factor of the relationship. Cooperation will also involve the fields of science, technology, innovation, environment protection and energy, culture [Romanian Government, 2013].

The increasing Chinese investments in Hungary and Poland, the recent developments involving the China-Romania relationship as well as the overall activism exercised by Beijing in Central Eastern Europe are causing raising worries at the core of the European Union Institution. De Gucht's statement before the China-CEE forum, with the EU commissioner for trade strongly recommending to make no concessions to

Beijing during the negotiations and outlining that China should not be the center of the EU external and trade policies, offers a clear example of such worries. CEE countries replied sharply but both Li Kenqiang and Victor Ponta stated that good China-CEE ties should strength the overall China-EU relationship. Ponta, in particular, called the *high-level meeting as a complementary effort to the general framework of the strategic relations between the European Union and China* [Actmedia.eu, 2013]

Nevertheless, the increase of Chinese investments in Europe spreads the feeling of insecurity with regard to Beijing's real aims. As above mentioned, the main question is if the Chinese investments are the result of purely economic calculations or political goals are behind them. The fact that most of Chinese investments are realized by State-Owned Enterprises (SOEs) feeds these fears, as well as does the experience of Chinese FDIs in Africa and Latin America Caribbean that ensure support for Beijing's stances in various international fora.

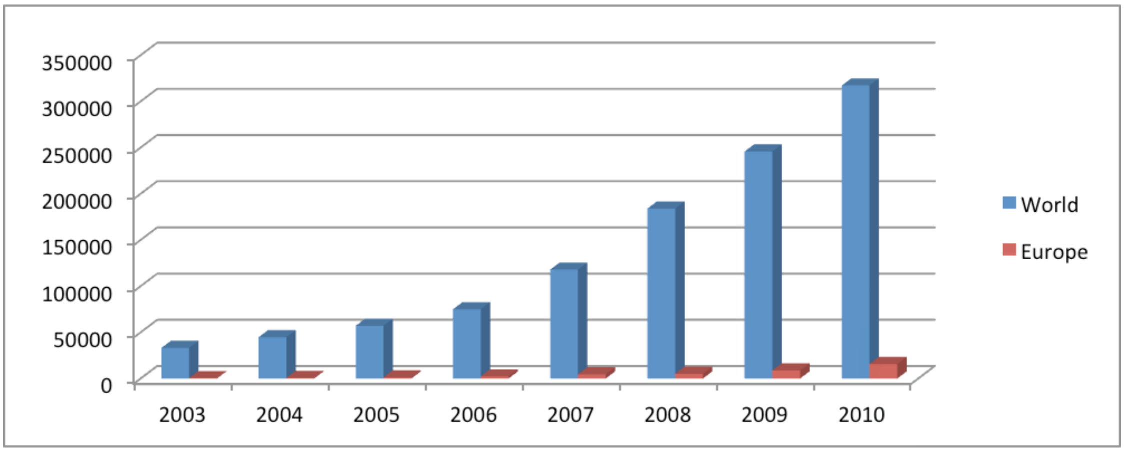
Following the output of the China-CEE forum held in Warsaw in 2012, when former Prime Minister Wen Jiabao promised $ 10 billion credit addressed to the CEE countries, someone in Europe started to talk about a "Divide et Impera" strategy. According to Bolzen and Erling [2012] China is trying to create subtle dependencies with individual EU countries, dividing the EU new members from the old ones. Golonka [2012] highlighted that China is "*playing member-states against each other and against their own collective interests*". Meunier [cit.] has noted that the supposed "Divide et Impera" strategy is put in place through the investments: "*In order to attract Chinese FDI, EU countries are employing a variety of methods which put them in competition with one another. They use national investment promotion agencies. They use national incentives, from taxation to social policies. And sometimes they free-ride by offering very lax, if not non-existent, regulatory conditions for entry*". According to Meunier [2014], therefore, Chinese investments might cause a race to attract them among the European Union member countries. The division of the EU members in such a race, however, does not seem the Beijing's real intension.

Turcsanyi [2014] outlined that the CEE countries cannot sustain alone the bilateral relationship with China as some of the bigger EU countries do (perhaps not always successfully). Others noted that CEE economic diplomacy towards China is not satisfactory, because "*CEE tends to think in the short term. Economic diplomacy as well as corporate partnership building are in their infancy*" [Golonka, cit.]. Alexandru-Ioan Miloșan and Wang Xueyu [2012] argue that Romania could do more with its relationship with China, but Bucharest appears prudent because the EU is suspicious. Actually, all the CEE countries are working more on the commercial field than on the investment sphere, promoting their products in China, an effort aimed to reduce the imbalance of the trade balance. Such promoting activity performs mainly through the participation to international fairs and exhibitions but does not seem to be effective. CEE countries' leverage is too weak and their exporters face three main problem: they do not know sufficiently the Chinese market, they miss and do not understand the *guanxi* system of relations, they lack expertise and credibility. Some CEE countries are trying to enhance its bilateral relationship with China through a specific agenda, such as Poland and Hungary. Warsaw recently launched the "Go China" policy, catching some good results in attracting Chinese interest, as well as Budapest is implementing an "Opening to East" policy focused not just on China but on the whole East Asian region. In the investments field, however, CEE countries' economic bilateral diplomacy lays behind.

Indeed, Turcsanyi looks to the CEE group as a platform that would provide the necessary support to face the growing relationship with Beijing. If EU institutions are not happy about such development, the Czech scholar argues, "*it may be questioned who is, in fact, drawing the division lines in Europe*". Moreover, Takacs [2013] notes that "*it may not be very beneficial for an economy as big as China's running for a low percentage of market shares in a single CEE country*". The consequence is that China is not pursuing a "Divide et Impera" strategy. Not intentionally at least. Beijing is just consolidating and developing bilateral relationships and the muddle about its FDIs in Central Eastern Europe is just a consequence of European disunity and current economic crisis.

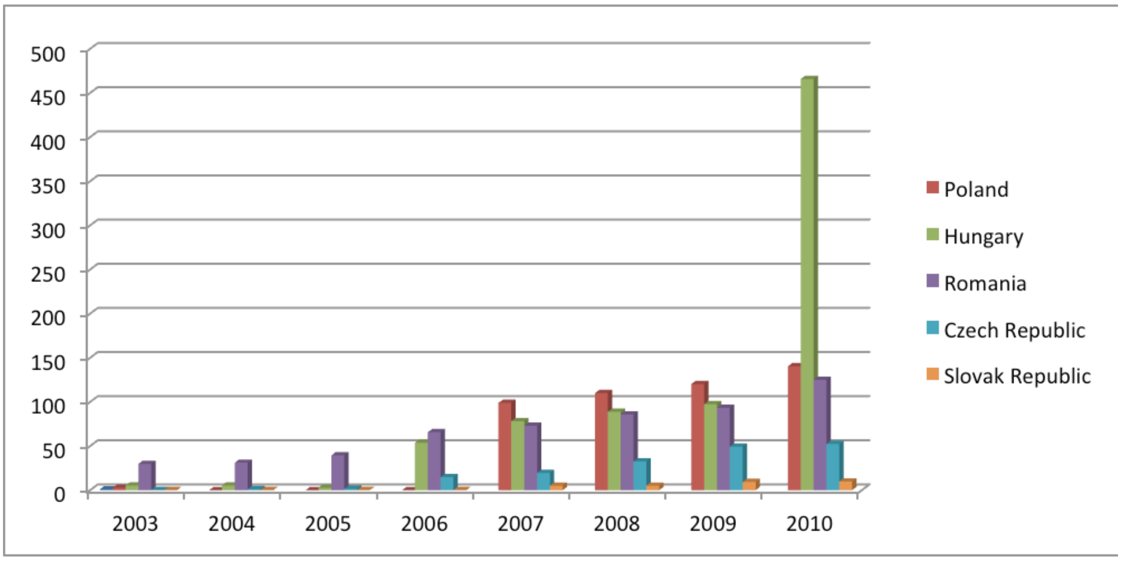
The China-CEE forum, however, is undoubtedly a Chinese creation. So, if China does not intend to divide European Union, why should it create a new arena for bilateral discussions instead than dug deeper with the EU-China bilateral negotiations? The point is that China might gain a lot from these divisions and acrimonies, of course. Nevertheless, Beijing could gain more by negotiating with a unite and friendly EU instead than a hostile and divided Union. After all, CEE countries are tiny ones and their bargaining leverage inside the Union is small. Thus, through the creation of a CEE group of countries, China is probably trying to allow them the leverage that they lack singularly. The final goal, therefore, is not just to earn advantages from economic negotiations but to influence the choices of the EU central institutions on foreign as well as internal policies by using the economic and political leverage exercised upon each member. Facing the growing competition with the United States, China needs the EU support on several issues emerging within the international organizations or from global emergences. On the internal sphere, it might lead the EU institutions to adopt a more and more Chinese-friendly legislation. It will take long time, for sure, but some positive output is already visible: on the issue of the embargo on supplies of military equipment, for example, some EU members turned to be favorable to its abolition. Eventually, Chinese politics towards Europe are not hegemonic. They could not be. Despite the huge economic relationship, Europe is not at the core of the Chinese interests. Europe is important for China, of course, but in a way addressed to balance United States power in the global arena. Thus, hegemonic politics such as the "Divide et Impera" one could be counterproductive for Beijing. Bilateral talks with each EU members aim to make pressure on European institutions to adopt a China-friendly attitude. And CEE countries can be the key to prove the Chinese politics successful.

*Chart 1. Chinese FDIs outward. $ millions*



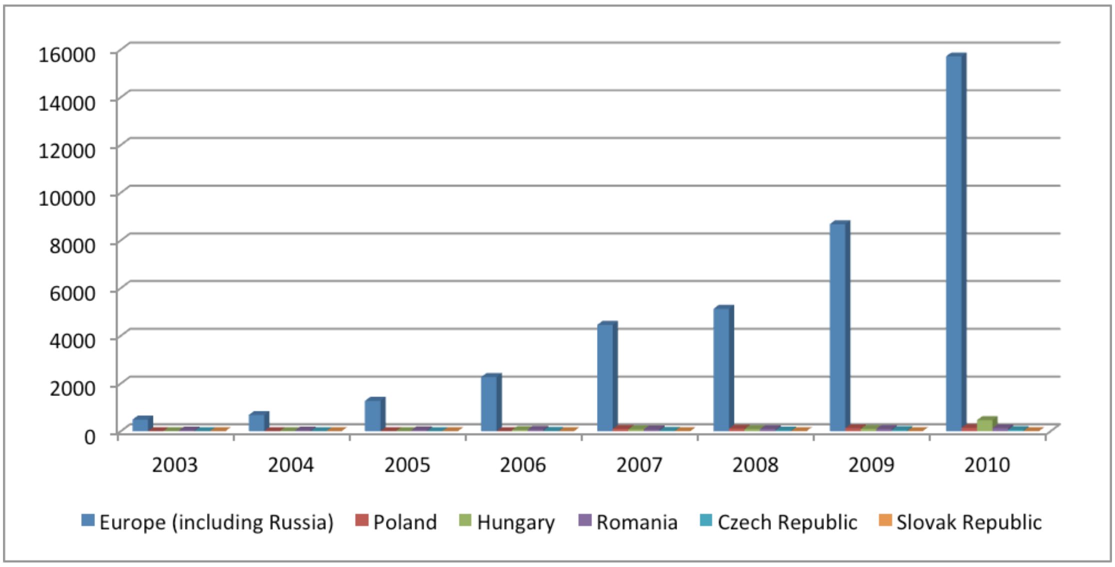

Source: MOFCOM

*Chart 2. Stock of non-financial Chinese FDI in CEE countries, 2003–2010. Data on million US$*



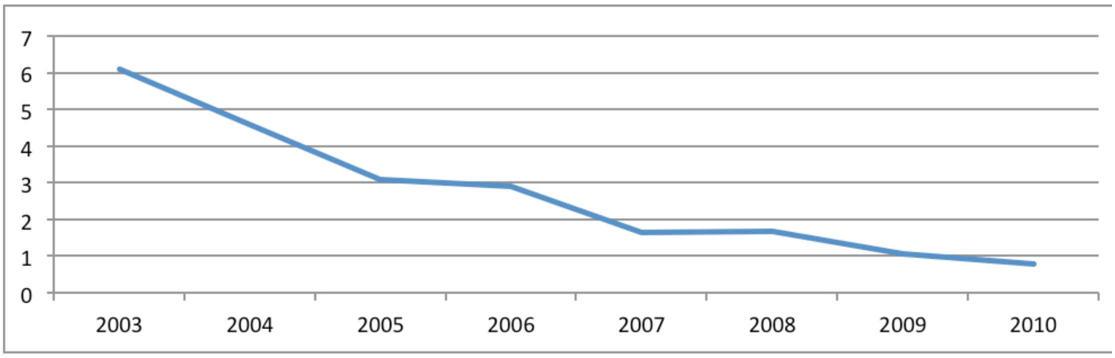

Source: MOFCOM

*Chart 3. Stock of non-financial Chinese FDI in Europe and CEE countries, 2003–2010. Data on million US $*




Source: MOFCOM

*Chart 4. Decline of Romania's percentage in Chinese FDIs to Europe*




Own elaboration of MOFCOM data

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