CHINA'S ATTRACTION: THE CASE OF CENTRAL EUROPE

Edited by Csaba Moldicz

Oriental Business
and Innovation Center
OBIC

BUDAPEST BUSINESS SCHOOL
UNIVERSITY OF APPLIED SCIENCES
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Preface

The Oriental Business and Innovation Center (OBIC) was set up by the Budapest Business School, University of Applied Sciences and the Central Bank of Hungary in 2016. One of the main goals of the initiative was to contribute to a better understanding of Asian cultures, economies, and languages in Hungary. OBIC's activities encompass three pillars: the improvements of language skills of our students, enhancing academic mobility towards Asia, and support of Asia-related research. This booklet is the first, but hopefully not the last fruit of our efforts, in making specific features of the Asian economies more penetrable by Hungarian audiences; however, in this case, we also hope to draw attention to the investment and trade opportunities offered by Central European countries.

The change in the perception of China is not a new phenomenon; this had already been observable after the turn of the new millennium, when the rapid growth of large, emerging countries and the shift in economic and political power became more and more obvious to analysts and policy-makers. It is not a coincidence that the term BRIC-countries was coined by Jim O'Neill in 2001. Since then, the notion that the robust growth of large, developing countries could counterbalance the falling demand in advanced countries, contributed to significant adjustments in economy policies. In the meantime, China has turned into a middle-income country, thus becoming the greatest success story in the last wave of economic globalization. That is why it must not surprise us that in recent months, China has turned out to be the proponent of globalization.

The One Road, One Belt Initiative, along with the New Silk Road, and the 16+1 mechanism are all integral parts of China's economic and globalization strategy. These initiatives to open up new markets for Chinese goods and services are welcomed by Central European countries, which have always had to try to balance between the big powers, while also in constant need of capital and technology. Historically, the capital and technology flowed from Western European countries to Central and Eastern Europe, thus generating growth but also asymmetries. The Central European dependency can be mitigated by China stepping up its economic presence in the region.

The authors of this book attempt to analyze the most important impacts of the growing Chinese presence in the region. The first chapter[1] of the book analyzes the nature of the attraction China has on the Central European countries, and it concludes that "… Chinese efforts to enhance economic cooperation with the CE region might have been motivated by the rising political power of China, but because of the minimal political importance of Central Europe for China, this cooperation cannot be solely built on political interests." At the same time, the author emphasizes a neglected point in the discussion around China's role in Central Europe. He contends that one of the "best-selling products" of China is the Chinese developmental state model or in other words a model in which the state intervenes, does not restricts itself to the regulation of the economy.

The second chapter[2] of the book gives an overview of Chinese efforts to broaden trade and investment ties through diverse regional integrational forms. On the hand, the author draws the general conclusion: "the answer to the transformation process in the global economy will be an increase in regionalization trends." On the other hand, when it comes China's role in the regionalization trend, he emphasizes "China intends to encourage regional consolidation of peaceful coexistence. Its political and economic objectives are not in conflict. The advanced countries however, have been watching China's movements with concern." The irony of the story is that China has been the fighter for free trade in recent months, while countries like the US, and the United Kingdom – historical proponents of free trade – seem to adopt increasingly protectionist arguments and trade measures in order to protect their domestic markets.

The third part of the book[3] undertakes a critical analysis of the One Road, One Belt Initiative (OBOR-Initiative). The author emphasizes the difference between Central European countries with regard to their willingness and capabilities to take advantage of the OBOR-Initiative. He contests that "The major issue is the lack of reciprocity between the two sides. While Chinese companies can easily act on the soil of the EU, European companies have to face many official and unofficial obstacles in China. Fair competition is still far from becoming a reality as the Chinese state offers subsidies and other kinds of support to its companies. The EU should be strict on the rules of level playing field, and a bilateral investment treaty may help to achieve European goals."

1 Csaba Moldicz: The Attraction of China in the Central European Countries - Practical and Theoretical Considerations
2 Pál Majoros: China in the Network of Regional Integrations
3 Tamás Matura: Chinese Investment in the EU and Central and Eastern Europe

The fourth chapter[4] focuses on trade relations between the EU and China in a unorthodox way since the author draws attention to the EU's well-known vulnerabilities from historical perspectives. He argues that "The six historical parallels introduced in the paper are divided into two categories that cover internal problems and external challenges for the EU in its relations with China." He emphasizes historical parallels: the European trade deficit against China, the fear of the Sino-centred tributary system's modern era revival, the divisions of European nations, and the fading European presence, etc.

The last chapter[5] of the book analyses the parallels in the functioning and regulations of the Chinese and the Hungarian Central Banks. Based on the historical changes in the Hungarian Central Bank's functions, the paper tries to draw conclusions with regard to possibilities of modernization and liberalization within the Chinese Central Bank.

We are thankful for the financial assistance of the Central Bank of Hungary, the Ministry of Human Capacities (Program of Excellence), the leadership of the Budapest Business School and all the people who helped the birth of this booklet - the first in the Oriental Business and Innovation Center Book Series.

The editor of the book:
Csaba Moldicz

4 Ambrus Gábor Szentesi: Trade Relations Between the EU and China and What History Tells Us about Them

5 Péter Bihari: Institutional Challenges to the Central Bank of China – a Central European Perspective

A Few Words about China's New Role in the Central European Region

Csaba Moldicz

The paper aims to briefly overview Central European initiatives taken after 2008-2009 to boost Chinese and Central European economies. It raises the question as to how or whether these Chinese economic efforts can be interpreted in the light of hegemony theories. The paper concludes that Chinese efforts to enhance economic cooperation with the CE region have been motivated by the rising political power of China, but because of the minimal political importance of Central Europe for China this cooperation won't be stable if solely built on political interests. Albeit mutual economic interests would be vital to the stability of the cooperation, it faces serious challenges, since Central European countries have vital interest in job creation and access to new technology, whereas logically the Chinese state encourages domestic firms to go global, because of the need new markets and upgrading the Chinese economy. The paper argues that one of the "best-selling products" of China is the Chinese developmental state model which is, for the time being, in high demand among Central European countries. This "product" challenging the free-market based democracy model is the most important element in the cooperation with China.

1. Introduction

In the aftermath of the Global Financial Crisis, experts argued that China's resilience in the face of external financial shocks had the potential to mitigate the devastating effects of the economic crisis in Central Europe effectively. This argument implied the great potential of Chinese demand due to the growing purchasing power of Chinese middle-classes. Others pointed to the economic interests of the raising political power. The economic efforts of a politically and economically raising China take shape in five different areas now: trade, investments, the One Belt, One Road initiative, multilateral financial institutions, and the internationalization of RMB.

Although trade and investments might be hampered by a slowdown in the Chinese economy for a very short period, the four remaining areas are unlikely to be affected by the cooling economy in China, since the slowdown is of temporary nature and much of these initiatives are motivated mainly by political considerations. The other side of the coin is that most Central Asian countries responded positively to Chinese initiatives, and have a clear positive attitude towards Chinese investments, mainly related to the One Belt and One Road initiative. These countries need Chinese investments to counterbalance the Russian political and economic influence. Most of the Central European countries also walk a tightrope balancing between their own economic and political interests. For them, more economic integration means reduced sovereignty in an 'ever closer Union'. Thus, these countries also need Chinese investments to offset Western European political and economic interests. However, it is obvious that each and every one of them faces very different challenges, since they are part of the Single Market and receive substantial funds for economic development. Cooperation with China is a long run economic interest of Central European countries, while access to EU-funds will be more limited after 2020.

Since 2008, there have been several initiatives, academic conferences, and political meetings to encourage various forms of economic cooperation between China and the Central European region. In addition, Central European countries have adjusted their economic policies to the new realities of the world economy, and have launched new trade and investment strategies towards China.

The reason, why did these countries adjust their economic trade and investment strategies, can easily be shown through the change in FDI patterns. In the late 1990s, China grew to be the most important destination country of foreign direct investments, and in the new millennium it also became the second largest holder of U.S. bonds, recently owning 1049 billion USD.[1] The country also developed into the second largest exporter of FDI in 2014 which vividly shows the depth of structural changes in the world economy. The Chinese diversification strategy includes investing a significant share of abundant capital rather in high-yielding shares and corporate bonds than in secure, but low-yielding US bonds, however, it must be said that the purpose of the diversification is not only to invest money more efficiently, but also to tap natural resources and gain access to new markets and new technology. From this point on, opinions diverge in the question as to whether this diversification strategy also pursues political goals of the emerging hegemonic Chinese state or not. But if you look at the importance of African countries China began to cooperate more closely in the recent years, it is clear, economic interest must have been the prevailing interests since the countries are far away from being global players in the world politics.

1 November, 2016, US. Treasury data.

Another part of the Chinese strategy encompassed the stimulus program after the Global Financial Crisis, which was heavily criticized by some economists[2] referring to the low efficiency of these public investments. That is why it can be argued that along with increasing savings, surpluses, and a need for a structural change there is an ever-growing demand for more efficient investments, and improving profitability of the Chinese firms. And this need is often reflected in the internalization of large Chinese enterprises.

The majority of these outbound foreign direct investments (OFDI) are still directed to developing countries; however, the share of Chinese OFDI to Europe has been increasing in the recent years, which also shows the ongoing structural change in the Chinese economy. Hence, the Chinese investments in developing countries are rather resource-seeking investments, while OFDIs in Europe have already reflected the need to speed up the structural adjustment of the Chinese economy leading to higher added value goods and services.

From the point of view of the Central European countries, it is crucial theoretical question whether this economic rise will continue in the coming decades, China will be able to avoid the middle-income country trap. The so-called middle-income country trap refers to the problems of structural change of countries where economic strategy relies on cheap labor in the early stages of economic development, but in the next phase of development new comparative advantages have to be found since due to earlier success wages are on rise. This trap clearly poses real threats to the Chinese economy since economic successes pushed up wages, in particular in the South of China, reaching and exceeding average Hungarian wages. (In the Suzhou area, average wages vary between 3.000 and 8.000 Yuan, depending on skills.) In theory, there are other constraints and uncertainties to be considered.

1. Export have a relatively low domestic value added share,[3] but this is why one of the main goals of Chinese economic policy to move up the value chain. This is the very reason why Chinese investors target already existing firms, and the acquisition of technologies.

2. Whether "a hard landing" of the Chinese economy will take place in the near future or not at all is difficult to forecast with precision. There are very diverging

2 More details about the debate on how much of China's economic growth is driven by investments in infrastructure or by improving efficiency (Total Factor Productivity) can be found in Wu (2011).
3 In 2011 domestic added value reached 68 percent in China, 85 percent in the US, 74 percent in Germany and 85 percent in Japan (OECD data).

prospects for China's economy, for example: Elliott is sceptic about 'hard-landing', arguing "[...] anyone who has seriously studied China realizes that the leadership of the Communist Party and of the government is very smart and has analyzed the issues carefully. The path to power and wealth in China generally runs through the State and consequently most of the best minds compete hard for these positions." (Elliott, 2014) In contrast to him, Kenneth Rogoff skeptically warned in a BBC interview that hard landing poses a real threat to the global economy. He argued that the threat comes from a credit-fueled economy. (Marketwatch, 2016) But the truth is, that despite the 2014-2015 fall in manufacturing, the Chinese Caixin Manufacturing PMI by HSBC is well above 50 again! Another argument is that this change is in line with Beijing's efforts to shift the growth emphasis to domestic consumption and services rather than exports and government-led investment.

3. There are also external threats the Chinese economy is facing. The Trump Presidency will set American foreign policy and economic diplomacy on a new path, thereby it will reshape world politics and word economy in the coming four years. The American withdrawal from the Transatlantic Trade and Investment Partnership (TTIP) and other protectionist proposals will not only impact Chinese exports but they also indicate that world trade is likely to be affected by international politics adversely in the next years as well. Even though the change in American trade strategy might pose threat to the Chines economy, it can also offer opportunities to an emerging global political and economic power of China.

2. The Four Different Layers of Cooperation in the Central European Region

Despite above-mentioned uncertainties regarding the development of the Chinese economy, trade with the Central Europe and investments in and from the region are part of the diversification and restructuring strategy of the Chinese economy. Since the early economic reforms in China, it has been a clear policy goal to open up the economy in order to attract knowledge and capital. In the literature on the sequencing of foreign investments it is often emphasized that the period of inward directed internalization of the economy, which can be characterized by a rise in foreign direct investments, is usually followed by an outward directed internalization of the domestic market. During this period, domestic firms are able to enter the market, either in form of foreign direct investments, firm acquisitions, mergers, joint ventures, or through purchases of shares. The Chinese economy clearly entered this second phase during which outbound investments grow more and more important.

In early phases of modernization, the Chinese economic policy relied on "bring in" approach, emphasizing the importance of import and inward foreign direct investments as tools capable to increase the technological level of the Chinese economy, however after the turn to the new millennium "go global" strategies became more dominant in Chinese economic policy. The "Go out" policy was initiated in 1999 and implemented from 2001 onwards. There are different phases of the policy to be distinguished according to the State Council of the People's Republic of China:

1. In the first phase, many Chinese enterprises set up overseas sales networks, and they engaged in low-end international trade.

2. In the second phase, even state-owned enterprises tried to enter overseas markets, however, they mainly targeted areas where they could tap natural resources of the new markets (oil, natural gases, other natural resources) and these firms also engaged in infrastructure projects.

3. In the third phase of the "Go out" policy, large Chinese private firms began directly investing in foreign markets, set up factories etc. It must be stressed that this stage of internationalization not only includes moving low-added value manufacturing to neighboring cheap-labor countries, but also the acquisition of global brands like IBM or Volvo.

4. Based on Chinese government plans, the last stage of internationalization would lead to the dominance of Chinese private firms in this process. It would create a more diversified economy, and a better position within global value chains. To underline this trend, the State Council of the People's Republic of China quotes data of the Ministry of Commerce: "According to data from the Ministry of Commerce, Chinese non-financial investment in 2015 amounted to $118.02 billion, a growth of 14.7 percent year-on-year, and continuing growth in outbound investments over the past 13 years." (State Council, 2016)

As we could see, in the last phase of internationalization, acquisition of more and better technology are the explicit goals of the Chinese economic policy. Thus, the role of Central European countries in this internationalization can only be minimal.

Despite the uncertainties mentioned above and theoretical considerations with regard to the importance of Central European economies to China, it seems to be clear that trade with the CE countries and investments in and from this region are inevitable parts of the diversification and the restructuring of the Chinese economy. And the strengthening of trade and investment ties with China is also a necessary part of Central European efforts to boost economies of the EU. These ambitions have been very clear in the recent developments of the bilateral relations between the Visegrad Four countries (V4) and China.

Four different layers are to be distinguished in the relations between China and the V4 countries: (1) strategic partnerships, (2) regional frameworks, (3) the EU dimension and (4) global frameworks.

1. Strategic partnerships. Up to this point, there are two strategic partnerships initiated by China, one with Poland and the other with the Czech Republic. In the case of Hungary it is clear that Hungarian politicians promote the idea of a strategic partnership with China.[4] (Business Insider, 2016) The first-ever official visit of the head of China to Poland took place in 2004, it was followed by the official visit of a Polish head of state to China in 2011, where a strategic partnership of the two countries was established.[5] (Xinhaunet, 2012) In 2016, China also signed a strategic partnership agreement with the Czech Republic. Strategic partnerships are integral part of Chinese foreign policy, since China has established partnerships with 47 countries and 3 international organizations, with the EU, the ASEAN and the African Union. (Zhongping – Jing, 2014, pp. 18-19.)

2. The "16+1" mechanism. Despite efforts to strengthen bilateral relations, given the number of the Eastern countries and the relatively small size of the economies, it seems to be more manageable for the Chinese partners to establish regional cooperation frameworks. In 2012, another initiative was born by the launching of the "16+1" mechanism of cooperation including China and 16 CEE countries. And up to this point, each year a summit was held in different capital if the country group.[6] There are already positive signs of this cooperation as the quote puts: "According to the Chinese Ministry of Commerce, the total annual trade volume between China and CEE countries registered 43.9 billion U.S. dollars in 2010, and the figure surged to 60.2 billion dollars in 2014. China has plans to double its trade with the region by 2019."[7] (China Economic Net). Between 2009 and 2014, Chinese FDI flows to V4-countries increased by 366 percent, while total Chinese OFDI only

4 http://www.businessinsider.com/ap-hungarian-leader-wants-strategic-partnership-with-china-2016-10
5 http://news.xinhuanet.com/english/china/2012-04/26/c_123037803.htm
6 In Warsaw, Poland (2012); Bucharest, Romania (2013); Belgrade, Serbia (2014); and Suzhou, China (2015).
7 http://en.ce.cn/main/latest/201603/27/t20160327_9841265.shtml

doubled. (217 percent). However, it is not clear that how much of this change in data can be explained by the strengthening of the regional cooperation framework. The "16+1" cooperation mechanism is an intergovernmental platform which is extended by working groups, forums and dialogues in various fields. (F. ex. China-Hungary-Serbia joint working group on transport infrastructure cooperation; China-CEEC Health Ministers' Forum, China-CEEC Literature Forum, and China-CEE Countries Political Parties Dialogue).

China's 'one-size fits all' framework has a few limitations, which are to be led back to visible fault-lines between the sixteen Central and Eastern European countries:

(1) Large economies are more able to take advantage of the cooperation, whereas small economies find it difficult to cooperate with China. Size also matters in trade.

(2) Political identity also differs widely among the 16 countries (membership in the EU, Single Market and the Eurozone)

(3) This new cooperation form triggered suspicion in EU institutions, EU countries as to what are the Chinese intentions with this mechanism, referring to the possibility of the divide and rule tactics of great powers.

3. EU-China partnership. There is another layer which only partly overlaps the "16+1" mechanism is the EU-China comprehensive strategic partnership, which started in 2003, however, it is based on several formal agreements between China and the EU. (See the High Level Economic and Trade Dialogue in 2009 or the 1985 agreement on trade and economic cooperation etc.) The partnership was complemented by the EU-China 2020 Agenda for Cooperation in 2013 encompassing four areas of cooperation: peace, prosperity, sustainable development and people-to-people exchanges. There are various causes for criticism when it comes to this layer of cooperation:

(1) Traditionally the EU has deep concern about civil and freedom rights in China (at the same time, EU-member don't have, they want to trade with China).

(2) At the same time, the 28 countries of the European Union – despite being part of the Single Market – offer different business and investment opportunities.

(3) EU institutions are slow in their responses to Chinese political and initiatives, given the fact that they represent 28 countries.

Against this backdrop, it is no surprise that the Chinese foreign policy has favored more limited forms of cooperation in the recent years (bilateral or regional frameworks), where interests can be formulated more precisely and adequately.

4. Silk Road and the 21st Century Maritime Silk Road. Through this cooperation channel China seeks to establish contact with countries of very different development levels and more continents. This Silk Road was initiated and is being led by China. The main reason behind this initiative was the need to push down transaction costs of negotiating processes. V4-countries with the exception of Poland have small economies and along with Poland they belong to middle-income countries. That is the reason why this cooperation was speeded up by the "Belt and Road initiative"[8] proposed by China with the aim to promote the connectivity of Asian, European and African countries.[9] References to the Ancient Silk Road are often made as these remarks deliberately seek to reinforce the open and peaceful nature of this cooperation form.

The explicit strategic goal of all Chinese initiatives is to strengthen economic cooperation possibilities, without wishing to interfere with domestic affairs of the participating countries. This is made explicit in the case of the "Belt and Road Initiative". The so-called "Vision and Actions on Jointly Building Silk Road Economic Belt and 21st Century Maritime Silk Road"[10] stress this aspect by adhering to the following principles: mutual respect for each other's sovereignty and territorial integrity, mutual non-aggression, mutual non-interference in each other's internal affairs, equality and mutual benefit, and peaceful coexistence.

These Chinese initiatives were followed by or coincided with several strategical changes in some of the Eastern European foreign trade strategies. The most obvious example can be found in Hungary where the "Eastern opening policy" was launched in 2011. The strategy was revised in 2012 by adopting a broader growth strategy (the Széll Kálmán plan[11]). The strategy points out the importance of trade and investment diversification. The goal is to double the export of Hungarian small and medium enterprises to the targeted regions whereas China, Russia and India are the most important partners of these regions. Details of this policy are described by Zsolt Becsey

8 The full name of the initiative is Silk Road Economic Belt and the 21st Century Maritime Silk Road.

9 See the full text here: http://english.gov.cn/archive/publications/2015/03/30/content_281475080249035.htm

10 It was issued by the National Development and Reform Commission (Ministry of Foreign Affairs, and Ministry of Commerce of the People's Republic of China).

11 http://index.hu/assets/documents/belfold/szkt_2_0.pdf

who explains that besides the establishment of trading houses in emerging markets, and the promotion of Hungarian firms, in particular small and medium enterprises, initiatives in the education and tourism sectors are linked to the core "Eastern opening policy". (Becsey, 2014)

3. Funds to Facilitate Economic Cooperation

As it can be seen, China has utilized an internalization strategy which is built on a multilayer approach in which not only global, regional, and bilateral elements can be distinguished, but also efforts to make use of economic power built on the vast reserves of the People' Bank of China. In 2015 the Chinese Premier underscored the following possible elements of future cooperation:

1. a full leverage of the 10 billion USD special credit line;
2. the possibility of setting up a 3 billion USD investment fund;
3. the possibility of an RMB fund for China-CEEC cooperation;
4. the aim to create a 16+1 multilateral financial company. (Keqiang, Li, H.E. 2015)

Reserves of the central bank also matter in the broader picture, since the Silk Infrastructure Fund launched in 2014 is to be capitalized by China's foreign reserves. While the Fund invests in business projects, the Asian Infrastructure Investment Bank, which was set up with a capital of 100 billion USD in 2015, lends money to projects of the One Belt, One Road initiative. (Poland is the only founding member from the V4 countries.)

The One Belt, One Road initiative not only includes European countries, but Asian and African countries as well, thus according to the plans China is going to spend around one trillion USD giving loans to about 60 developing countries via the China Development Bank and Silk Road Fund. After underwriting the construction of circa 900 infrastructure projects, the funds are to be transferred from the Chinese banks to Chinese firms, which will carry out the projects using Chinese labor and materials. The project faces the question of how to assess and manage financial risks in numerous uncertain economic, and regulatory environments. Poor countries are happy to take cheap Chinese loans at the expense of future generations, but the question remains whether they are going to be paid back to the already indebted Chinese banking sector.

4. China's Approach to the Global Economic Order – What is the Role of the "16+1" Mechanism in China's Global Strategy?

China's economic rise is a paradoxical one, since the economy itself is a leading one in size, but it is still in some aspects a developing economy. China's efforts to transform the global economic order have been low-keyed, because this duality does not make China able to sponsor this change. However, there are clear signs that China strongly supports the reform of the international system, and has two main reasons for doing this:

- current crises, tensions highlight the problems of the global economic and political order,
- the current system reflects the interests of a small set of advanced countries. (Wang, 2013, p. 72)

It can be added that the Brexit and the policy of the new American Administration (see the TPP) both showing a definite withdrawal from the current political and economic system create clear opportunities for the Chinese foreign and trade policy to reshape the existing frameworks.

There are several schools of thought as to how the emerging China tries to achieve the change in this framework.

1. Some argue that the Chinese economic reforms depend on its participation in the existing order, thus the country is not likely to challenge the system.
2. The other version points out that China has an interest in "soft balancing", which means a slow extension of the Chinese frontiers, in particular when it comes to the adjacent countries.
3. Clearly, the third concept is about an aggressive foreign and trade policy which attempts to achieve a sudden change in the global order.

Recent political and economic changes support the theory of soft balancing. It is clear that China as emerging political and economic power has a strong interest in reshaping the institutional environment and after the Global Financial Crisis, the country has become more assertive in its foreign policy and trade strategy, but these are very cautious and moderate steps.

For the time being, China offers an alternative model of development policy to the developing countries of Asia, Africa, South America and to the Central and Easter countries as well. In contrast to the Washington Consensus, the so-called Beijing Consensus develops a pragmatic approach to problems, whereas the Washington Consensus clearly contained a vison of the desirable political and economic order of catching-up countries. The US was often blamed for exporting the American values and societal and economic institutions (free market economy and democratic institutions.) However, this approach would have required a slow democratization of the countries in question which did not find support among local elites. Democratization in exchange for investment and trade was never required by the Chinese, strictly in the spirit of non-intervention.

In the developing countries, the Chinese approach promises cheap credits and infrastructure investments while not intervening in domestic issues. The same conditions are offered in the 16+1 framework, however, V-4 countries are in a very different situation, because being part of the Single Market means the implementation of EU rules related to the procurement system. Being part of the EU also offers access to the EU transfers which grants and no credits. And this is a different situation – many argues, since one doesn't know what will be the financing conditions after 2020, when the new EU financial framework is to be implemented.

There is another channel of influence, which is rather underemphasized in the literature. In contrast to a regulatory state concept of the Western world where states refrain from intervention in the market places, the developmental state of China intervenes in the market in order to achieve certain goals.

5. What Does the Developmental State Model Offered by China Look Like?

The developmental state paradigm refers to the effectiveness of these states in implementing policies aimed at modernizing, reorganizing backward and traditional economies, directing the behavior of economic players, and shaping major macroeconomic trends.

The term 'developmental state' describes one version of the free market economies, indicative of East Asian countries. This expression also refers to a state-determined, albeit more or less market-friendly, approach to economic development. Asian developmental states can generally be characterized by a strong emphasis on diverse forms of state intervention; however, these institutions differ to some extent in Japan, South Korea and China.

Originally, the developmental state concept only referred to Japan and later also to South Korea. Chalmers Johnson was the first to conceptualize the term 'developmental state'. He emphasized competent and far-sighted bureaucracy as a defining feature of the Japanese economic miracle. The purpose of making a distinction between capitalist and capitalist economies was to call attention to differences instead of similarities in these economic systems. As he puts it: "One of my purposes in introducing of the 'capitalist developmental state' into a history of modern Japanese industrial policy was to go beyond the contrast between the American and Soviet economies." (Johnson, 1999, p. 32)

Later, the concept 'developmental state' has become popular, and major contributions were made by Alice Amsden (Asia's Next Giant), Robert Waden (Governing the Market), and others. However, the emphasis was shifted in some cases, some analysts highlighted infrastructure, policy tools (saving and credit giving schemes, foreign investments, export zones, government interventions to spread technology etc.), history or culture. Among the Asian Tigers only Hong Kong adopted a free market approach. One of the often-recurring argument is that strong state is needed to mobilize resources for public goods, since only the strong state is able to convince people and firms that painful political adjustments are necessary to make an economic breakthrough. At the same time, politicians must have credible strategies in order to convince the actors of the private sector.

Macroeconomic and political stability are preconditions of economic success. Political stability often coupled with the ability to build strong and efficient institutions. In each of the cases, import-substituting policy was part of the history, however, it was short-lived. Another common element in the economic development of these countries was the importance of agriculture, which was not heavily taxed and agricultural workers were not impoverished. A strong social infrastructure of family, local communities supported by the culture, a modern physical infrastructure financed by governments and donors can be found in Japan, and South Korea. In each case, the 'benevolent' external supporter – the United States pursuing its own political and economic interests – is also there to aid the countries and advise the elites of these societies. These are the most important elements of the developmental state concept. In his 'Governing the Market', Wade ascribed the success of these Asian countries to two basic policies: very high levels of productive investment and exposure of many industries to international competition. (Wade, 1990, pp. 22-33)

Utilization of very similar economic policy measures can be clearly shown in the case of China. And results are plenty to be found in the modern China, so it might surprise us that Central European countries have been turning to the developmental state model in recent years, since it is clear adaption of Western European recipes for economic catchup did not bring the awaited results and the gap between Western and Central European has not diminished since 1990.

6. Conclusions – the Effects of a Successful Story

The "16+1" mechanism faces serious challenges with regard to differences in legal framework, but these are most likely to be solved. Other challenges arise from the fact that in terms of investments and trade Central European countries do not offer too much to China, and CE countries are far less important than the Chinese would set political considerations ahead of economic ones. However, China and its developing state model along with the so-called Beijing consensus has become very popular in some regions of Asia, Africa, Latin-America and Central and Eastern Europe. China has reinforced its attraction thanks to cheap credit, aid and the promise to improve infrastructure in the countries in question. That is clearly a soft power, whose attraction has gained many supporters in the recent years. As Josep S. Nye puts it: "Success depends not only on whose army wins, but also on whose story wins." (Nye, 2005)

As we could see the Chinese governing market approach is very different from the Western European approach where the state rarely intervenes in the marketplace. (Even among the so-called free market systems there clearly exist different versions.) What are the very basic elements of Chinese development which are to be connected to the first and the second wave of Asian developmental states:

- a stable policy environment which protects bureaucrats from external political influences. Relying on traditions, the Chinese state has been able to build such a stable environment. In Japan, the Ministry of International Trade and Industry, in South Korea the Economic Planning Board, and in China the National Development and Reform Commission are the institutions playing part in the creation of a favorable environment.

- At the same time, bureaucracy must have its ties to receive the needed feedback from the society.

- The third element is the relatively equal distribution of income, which not only brings about social peace, but also creates a growing aggregate demand for domestic products and services. This element might be the one China struggles the most with (Woodall, 2014).

When it comes to a new approach in the economic policy, which is being presented as alternative to the liberal, regulatory model, the Hungarian economic policy might be the one with the most "innovative" solutions including some features of the developmental state as well. Elements as

1. re-industrialization of the economy,
2. preference of domestic firms,
3. prioritizing selected sectors,
4. managing asymmetric imbalances,
5. dealing with indebtedness,
6. connecting taxation policy with economic priorities,
7. and efforts to strengthen state bureaucracy

clearly point to a more active role of the Hungarian state in the domestic economy. Besides the developmental state model China offers the Beijing Consensus as well, which goes back to one of the key lessons of the Chinese history: the Chinese state is susceptible to fall apart if politics is unstable. And politics tend to be unstable if there is no substantial and sustainable economic growth. So, political – internal or external – instability is interpreted as a threat to economic growth, since there is a clear connection between the two, influencing each other mutually. It is no surprise, then, that the Chinese recipe for economic cooperation, namely the Beijing Consensus, seeks to strengthen stability, emphasizing the "no intervention principle." The Beijing consensus highlights the following elements: (1) the importance of innovation (which is not new compared to the small Asian Tigers); (2) the rejection of the GDP per capita approach, putting emphasis on other indicators (HD index) and (3) the self-determination of countries, which puts the "no intervention principle" in the focus again (Habib, 2015).

The Beijing Consensus not only challenges the US dollar as a global reserve currency, and the establishment of the Asian Infrastructure Investment Bank creates a new competitor to the World Bank, but more importantly, the development model challenges the free-market based democratic model of the Western world by offering viable alternative to democracies. Thus, the paper concludes that China's efforts to enhance economic cooperation with the CE region can be traced back to the interests of a slowly rising political power, however the V4 are not geopolitically important enough to base this cooperation on exclusively political interests. That is why he author of this paper argues that the “bestselling product” of China is the Chinese developmental state model, a “product” which tests the vitality of the free-market based democracy model and can turn into a fruitful cooperation between China and the CE countries.

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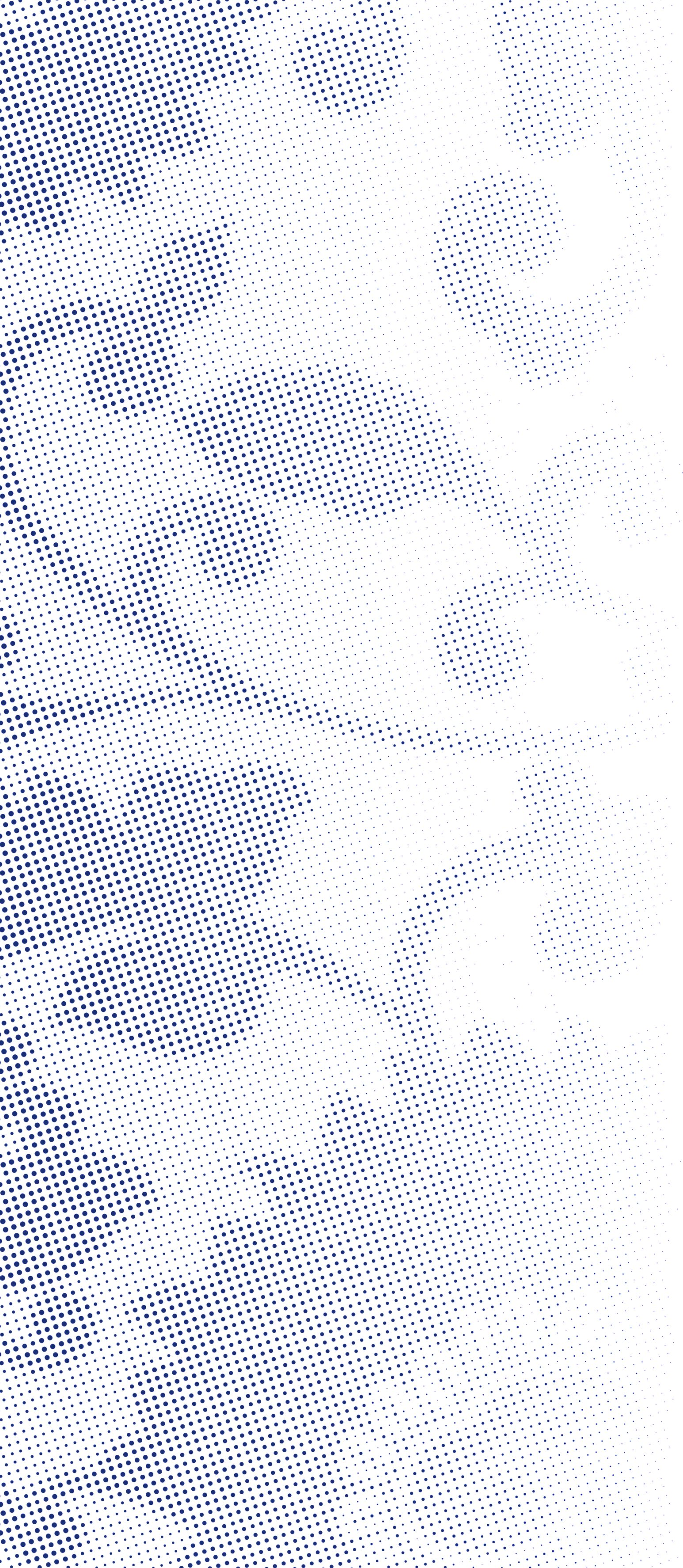

China in the Network of Regional Integrations

Pál Majoros

Possibly the most important change in world economy in the last 40 years has been China's entering into its new global position: having left its marginal situation behind, it has become the world's no. 1 exporting country and has also earned a second position right behind the US as to world output.[1] This fast development is a clear result of China's 'Reform and Opening' policy (Majoros 2011, pp. 178-191): in 1980, China's share in the world trade was slightly below 1 percent, while it reached 4 percent 21 years later, when the country joined the WTO, and 13 percent in 2016 (preliminary figure). Between 1980 and 2010, China's economy produced an average annual growth of 10 percent, but exports already exceeded 15 percent (Majoros, ibid). Chinese economy slightly slowed down in the following years, but exports growth seems to steadily exceed the country's economic growth. According to the IMF's and the OECD's forecasts, by 2030, China might also overtake the US in production. (In 2002, the National Congress of the Communist Party of China set this objective for 2049.)

Data show that China tripled its exports at the beginning of the new millennium. The fact that China joined the WTO in 2001 played a big part in this achievement, but its new politics and economic policy also helped the country to sharply increase FDI inflow. After 2001, for a short period of time, China was the No.1 destination country for foreign investment, otherwise it holds its strong second overall position behind the US. Capital inflow has resulted in the appearance of new modern technology, the expansion of employment, a massive increase in export capacity and also entailed an increase in budgetary revenues. But let us not forget that in China capital inflow strengthened free market thinking as well.

It is worthwhile to mention that China's WTO membership played an important role in the country's economic success. In return for the country's most favourable treatment and a preferential treatment for the trade of many of its products, China has significantly lowered its customs tariffs, opened up partly its market and also started to implement and apply the WTO's standards and regulations. However, a

1 The People's Republic of China will be simply referred to as China.

membership in the WTO does not necessarily mean that a given country's market economy status be automatically assumed. As a consequence of this, China's exports had to face anti-dumping procedures several times for alleged market disruption. At the beginning of the new millennium, the new trade policy is a clear result of the increased number of commercial conflicts and the discriminatory behaviour against China. Another reason for this was the fact that during the 2008/2009 world economic crisis many countries, developed countries as well, have implemented protectionist economic measures – leaving no other choice to China either.

1. Changes in China's Foreign Trade Policy

The earlier multilateral approach has been replaced by a bilateral one: due to the failure of the WTO Doha Round, the sustained uncertainty about China's market economy status, and the fierce competition between China and Japan for the No. 1 position in Asia, China has elaborated a new foreign trade strategy in order to become a centre of gravity for trade in the region. This change in the strategic thinking was partly entailed by the shift in US President Obama's strategic thinking: due to TTIP and TPP integrational negotiations between the EU and the US, China found itself in a situation where its foreign trade could suffer discrimination from developed countries. At the Asia-Europe Meetings (ASEM) the enlargement of trade relations is a central issue, which reflects the EU's will to intensify its foreign trade relations with countries of the South-East Asian region (during the first ten years, Central Asian countries were all absent from ASEM negotiations). This was interpreted by China as a manoeuvre being directed against its interest and it undertook to open negotiations with the countries of its region to conclude free trade agreements. It is important to underline that according to GATT/WTO regulations exemption from customs duties within the free trade area does not necessarily have to be expanded to other WTO member states as well. This was (and still is) an important reason why developed countries (EU, USA, Japan) apply the same method to improve their market positions. No space is allowed here to analyse how this process will affect the WTO,[2] but to be sure, it will contribute to the weakening of the multilateral frameworks.

Immediately after its accession to the WTO, China opened negotiations with the ASEAN countries in order to promote a free trade agreement. Moreover, the idea of a free trade area was first raised by Zhu Rongji, China's prime minister in 2000 during the China-ASEAN summit, even before the country's accession to the WTO. This

2 This issue is analyzed in detail in Kruppa 2016.

offer took many by surprise: one of its objectives could have been to meet ASEAN member countries' growing concerns about the potential economic impacts of China's 2001 accession to the WTO, while still underlining the mutual benefits (the win-win balance) of such a relationship. One of China's reasons could have possibly been its strive to gain a first-mover advantage against Japan in their competition for dominance.

In order to secure its trade positions, China has signed agreements for a broad economic cooperation with Hong Kong, Macao and Taiwan. These agreements were also followed by further agreements: at the end of 2016 China had 14 existing free trade agreements, 9 ongoing free trade negotiations and preparatory negotiations with 6 other partners. These agreements are not identical as China's trade diplomacy is mostly characterised by pragmatism in this respect: the content and the scope of each contract is in fact different. Agreements also incorporate dispositions as regard to the trade in products and services, investment protection, protection of origin and the avoidance of double taxation (this is the reason why the acronym RTA [Regional Trade Agreement] occurs more and more often in the literature, having a slightly different focus than the previously used FTA (Free Trade Agreement). Hilpert (2014) believes that bilateral, regional cooperation cannot be regarded as an alternative to the world trade system (WTO), but should rather be perceived as a complement to this. I cannot completely agree with this view as changes on the global scene show that all world trade operators have turned to bilateralism. WTO is still functional as a global framework, but its members increasingly seek to use backdoors in order to improve their respective positions. Such bilateral agreements enable countries to increase the scope of the trade in products and services, maintain their market benefits in the region and secure their imports of raw material and energy carriers. China is doing the same: besides strengthening its economic position in the Asian cooperation, thanks to such bilateral agreements, it can also hope to strengthen its political impact, improve cooperation with its neighbours based on mutual trust and reduce the fear of China. It seems that China's competition with Japan for the leading economic position in the region is fait accompli, but Japan still seeks to improve its positions through signing bilateral agreements, this is why potential free trade agreements are currently being discussed with the EU and the US. During the first week of his presidency President Trump pulled out of the multilateral TPP and offered to several countries, including Japan, the possibility of a bilateral free trade agreement. China has not been idle: it has reiterated its previous initiative on a multilateral solution: the RCEP (Regional Comprehensive Economic Partnership) which would become an agreement between the ASEAN+6 countries (China, Japan, South Korea, Australia, New Zeeland and India). This is a completely logical step from China: if free trade negotiations between Japan and the EU, Japan and the US as well as between the EU and the US are successfully completed, this would necessarily reduce China's market share. These negotiations also put pressure on China's economic diplomacy to broaden its economic leeway through signing further bilateral or multilateral agreements.

Table 1.

China's free trade agreements

Domestic agreements[3]	Multilateral agreement	Bilateral agreements	Preferential agreement	FTA projects (under negotiation)	FTA projects (under consideration)
China – Hong Kong CEPA (Closer Economic and Partnership Arrangement) China – Macao CEPA China – Taiwan ECFA (Economic Cooperation Framework Agreement)	China – ASEAN FTA	Developed countries: China – Australia FTA China – New Zeeland FTA China – Singapore FTA China – South Korea FTA China – Switzerland FTA China – Iceland FTA China – Chile FTA	APEC (Asian Pacific Economic Cooperation)	Multilateral projects: RCEP – Regional Comprehensive Economic Partnership, ASEAN+6 China – Japan – South Korea FTA China – GCC (The Gulf Cooperation Council) FTA	China – Colombia FTA China – Fiji FTA China – Nepal FTA China – Mauritius FTA China – Moldova FTA China – India RTA
		Developing countries: China – Peru FTA China – Pakistan FTA China – Costa Rica FTA		Developed countries China – Norway FTA China – Israel FTA	
				Developing countries: China – Maldives FTA China – Georgia FTA China – Sri Lanka FTA China – Pakistan FTA (second phase)	

Source: http://big5.mofcom.gov.cn/gate/big5/fta.mofcom.gov.cn/

3 Due to the 'one China' principle.

2. China's Free Trade Agreements

2.1. Domestic Agreements

After its accession to the WTO China was focusing on agreements with its so-called 'domestic' regions. Sovereignty was transferred to China in 1997 for Hong Kong and in 1999 for Macau. Both islands presently belong to the People's Republic of China while they have maintained their international legal subjectivity and their respective memberships in international organisations. Their unique situation based on the 'one country two systems' principle enabled them to sign an agreement with China as autonomous economic and commercial entities. These were the very first free trade agreements for China labelled as CEPA (Closer Economic Partnership Arrangement) and signed in 2003 with both territories. After a short transition period the arrangements guarantees exemption from customs duties for the trade of the so-called derivative products and partners undertake not to initiate anti-dumping procedures against each other. As to the trade in services, they mutually offer preferential benefits especially favourable to providers coming from Hong Kong. The agreement also guarantees the free movement of capital. Hong Kong and Mainland China are the most important trade partners for each other, furthermore, Hong Kong is the world's top capital exporter and importer as well. However, this latter status also raises the problem of round-tripping capital: capital makes a circle starting from China through Hong Kong, and gets finally back to China again, this time as foreign capital (this movement is generated by benefits granted to foreign owned companies). In the international statistics, it increases the related figures for China. But this agreement is beneficial for Macau too, and for its finance, services, tourism and gambling (casino) sectors in particular.

In 2010 China and Taiwan signed an ECFA (Economic Cooperation Framework Agreement), which essentially consists of a set of mutually preferential agreements: both partners undertake to lower their duty rates and remove trade barriers. The agreement is extended to trade in goods as well as to the service sector (financial and healthcare services, education etc.), and it also includes the free movement of capital. Besides its mutual economic benefits, through raising the dialogue between the two Chinas to a higher level, the agreement becomes of utmost political importance. The conclusion of the agreement also means that both sides approve the status quo through accepting existing borders. As a result of the agreement capital can flow directly from the island to China (while earlier it had to go through Hong Kong), and a big part of labour-intensive production was outsourced to the People's Republic of China. This plays an important role in the increase of Chinese exports.

2.2. China – ASEAN Agreement (CAFTA)

Chronologically this was the very first agreement and thus of utmost importance for China. In November 2002, the leaders of 11 states signed a Comprehensive Economic Cooperation Framework Agreement. The contract entering into force in 2005 also envisages the liberalization of trade between China and the ASEAN countries. Market opening and liberalization are the outcome of a process of many years which includes the following provisions:

- a process of reduction of customs duties and the progressive elimination of non-tariff barriers,

- the progressive elimination of barriers for trade in services,

- measures to guarantee the free movement of capital.

- special and differentiated treatment with regard to less developed ASEAN countries (as to non-WTO member states) China also ensured the most preferential treatment as well as enabled an asymmetrical dismantling of the customs duties – by 2010, with the exceptions of a few sensitive products, customs duties have been practically eliminated between the more developed ASEAN countries and China, while for less developed ASEAN states they have not been eliminated until 2015.

CAFTA was officially launched the 1st January 2010 guaranteeing the free movement for 90 percent of the products between China and six ASEAN countries (Brunei, Indonesia, Malaysia, Thailand and the Philippines). China's average customs tariffs for ASEAN products decreased from 9.8 to 0.1 percent, while the six ASEAN countries lowered their customs tariffs imposed on Chinese products from 12.8 to 0.6 percent. By 2015, Vietnam, Laos, Cambodia and Myanmar, that is the four new ASEAN member states, have completed the requirements for introducing an exemption from duties for 90 percent of Chinese products.

CAFTA currently encompasses 2 billion people. Behind the EU and the NAFTA, it is to become the third largest free trade area in the world (Lukács, 2012). This agreement is essential for China: it provides a huge market for Chinese products, plus ASEAN countries are also important providers of minerals and energy carriers. In the last 4 to 6 years ASEAN countries – the Southeast Asian region and the less developed countries in particular – have been an important regional destination for Chinese capital investment. Besides geographical proximity, this phenomenon can also be explained by wage disparities between the countries. As wages keep growing in China, it is more and more difficult to channel new but skilled workforce into production. This is the reason why the outsourcing of highly labour-intensive production to countries with low wage levels (Vietnam, Laos, Cambodia, and Myanmar) has started. Besides cooperation between the countries concerned, products and producers of China and the ASEAN countries face fierce competition from each in third country markets.

It is also important to note that shortly after signing the agreement with China, ASEAN countries have also concluded a similar agreement with Japan and South Korea. In addition, they have also signed different agreements with Australia, India and New Zeeland. Hence, ASEAN has become the part of a trade cooperation which encompasses close to one half of the global population. This demonstrates that ASEAN is the main engine of the integration in South East Asia.

2.3. Bilateral Agreements with Developed Countries

Chile was the first OECD country to conclude an agreement with China back in 2005 (it is interesting to note that official Chinese documents tend to refer to Chile as one of the developed countries). Customs agreement relates to the trade in services. From 2015 onwards 97 percent of the products move freely between the two countries. Negotiations on the movement of capital are under way.

A Regional Trade Agreement was signed with New Zeeland in 2008. New Zeeland has been the first developed country to approve China's economic system as a functional and competitive market economy. A free trade agreement was only signed with Australia in 2014. Besides the trade of products and services both agreements concern the free movement of capital as well. In this framework, particular attention is paid to the trade of agricultural and fisheries products.

Iceland was the first ever European country to grant recognition to China as a functional free-market country. A free trade agreement between the two countries was signed in 2013 which concerned products, services, protection of origin, intellectual property rights and movements of capital. In the very same year an agreement, basically similar to that between China and Island, was concluded with Switzerland. It is worthwhile to note that Switzerland is the only European country to have a marked trade surplus against China (owing to Swiss luxury goods exported to China). Both countries are EFTA members. Negotiations with Norway, also an EFTA member, are under way.

Singapore was the first Asian country to sign a bilateral free-trade agreement with China. The particularity of this agreement stems from the fact that Singapore is also a member of the ASEAN, which means that it also has links with China trough a multilateral agreement. Yet, bilateral agreements urged both countries to eliminate customs duties and speed up the liberalisation process as to trade in services and the movement of capital. Bilateral negotiations with South Korea started in 2012 and were successfully concluded in 2016. This agreement shares many common traits with the EU – South Korea free trade agreement (2011), and it also concerns the trade in products and services and the free movement of capital. China encourages the importation of advanced technology and services, preferentially involving FDI from South Korea.

2.4. Bilateral Agreements with Developing Countries

China signed an FTA agreement with Pakistan in 2005, focusing on the trade in products, but it also concerned trade in services and the movement of capital. The importance of the latter stems from the fact that Pakistan has recently become a key destination country for Chinese capital investments. Negotiations on investment protection and the avoidance of double taxation are still under way (second phase of FTA negotiations).

A free trade agreement was successfully concluded with Peru in 2009 with the objective to realise the free movement of products and the progressive elimination of customs duties. Negotiations on trade in products and the free movement of capital are under way.

Costa Rica was the first Central American country to conclude a bilateral agreement with China. As the country has a marked trade deficit against China, its most important trading partner, it urged China to lift barriers for its products (mostly agricultural products, coffee and banana). The agreement also concerns several areas of trade in services.

2.5. Preferential Agreement: China – APEC

APEC was founded in 1989 as a cooperation between 12 – presently, it has 21 members, which are: the US and Canada; the two North American members of NAFTA; Chile and Peru from South America; Australia and New Zeeland; Japan, South Korea, Russia and the 7 ASEAN countries (Brunei, Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam); and Papua New Guinea from Oceania. The three Chinas (the People's Republic of China, the Republic of China /better known as Taiwan/ and Hong Kong) joined this loose coalition of countries in 1991, which rather was a preferential area, a loose forum for consultations. The free movement of goods and capital was set as an objective in 1994, later reaffirmed in 2014. This integration is a typical example of new regionalism: its 30-year-old history is characterised by the cross-border economic cooperation of developed and developing countries (with no particular interest in politics and human rights). From our point of view it is worth noting that APEC is home to several functional regional integrations (NAFTA, AFTA, the bilateral agreements of ASEAN and the free trade agreements of Australia and New Zeeland included). Raising the existing bilateral and multilateral agreements to a regional/plurilateral level could further the formation of a free trade area, yet we have to take into account that Russia and Papua New Guinea are not involved in regional co-operations.

China has signed free trade agreements with 14 out of the 20 other APEC countries (the ASEAN members, Taiwan, Hong Kong, Australia, New Zeeland, Chile, Peru and South Korea), and similar negotiations are under way with Japan. China has no such agreement with the three NAFTA countries, Russia and Papua New Guinea.

2.6. FTA Projects

2.6.1. FTAs under Negotiation

Multilateral projects are of utmost importance. The importance of the Gulf Countries (Bahrain, Kuwait, Qatar, Oman, Saudi Arabia, United Arab Emirates) lies in particular in the fact that they are major oil exporting countries, important suppliers to China which has a trade deficit against most of them. In return for its opening-up policy, China expects from these countries to show similar signs of openness. Nevertheless, it has to be stated that this relation between China and the Gulf Countries is based on an asymmetric dependence as it is more important to China than vice versa.

China – Japan – South Korea FTA: multilateral negotiations started between the three economically most dominant countries in East Asia, which, besides trade and economy related issues, also concern political matters. Relations between China and South Korea, just as those between Japan and South Korea, seem to be more or less in order.[4] However, crucial issues tend to occur time to time between China and Japan: historical debates after World War II are far from being completely settled; island disputes (Spratly Islands, Senkaku Islands); construction of artificial islands in South China Sea; and in addition to this, it is also worth noting that Japan has a massive and constant trade surplus against China. Negotiations have been recently revolving around more political than trade related issues, as Japan has been improving its free trade network in diverging directions. TTP negotiations initiated by the US (to which Japan had already committed itself) have had rather negative impact on the economic dimension of the trilateral negotiations.

As it was already mentioned, President Trump had pulled out of the multilateral TPP. Now all countries are making calculations to find the best possible solution for each and one of them from an economic as well as a political point of view: either they engage in bilateral agreements with the US, or they rather opt for the RCEP – Regional Comprehensive Economic Partnership encouraged by China, which latter would result in an ASEAN+6 integration (the 10 ASEAN countries + China, Japan, South Korea, India, Australia and New Zeeland). It goes without saying that China, being excluded from the TTP, argues in favour of this latter option through which it could increase its political influence in the region. All ASEAN countries have already signed mutual bilateral free trade agreements, while besides the 10 ASEAN countries China already has agreements in force with Australia, New Zeeland and South Korea. The country also has ongoing negotiations with Japan, and preparatory measures are being taken for further negotiations with India. We will await further developments with interest.

Among developed (OECD) countries China has ongoing negotiations with EFTA-member Norway. China has already successfully concluded free trade agreements with two other EFTA countries: Switzerland and Iceland. Experts believe that the agreement between China and Norway will be concluded as soon as they reach an agreement with regard to fishing and trade in fisheries products.

Free trade negotiations between China and Israel are under way, which besides issues related to trade in products and services also concerns the movement of capital and particular attention is paid to the rules of origin. Among developing countries China has ongoing negotiations with the Republic of Maldives, Georgia and Sri Lanka.

4 However, disputes over deployment of the Terminal High Altitude Area Defense (THAAD) on Korean soil between China and South Korea has led to damages in the trade relations of the two countries in recent months. (Editor)

2.6.2. FTAs under Consideration

China is currently undertaking preparatory measures (ex. feasibility studies) for free trade negotiations with several countries. The case with India is of utmost importance: it is the world's second most populous country, it is a neighbouring country as well, and it has a 3rd position in global production adjusted for purchasing power (ahead of Japan). India's situation is far from being similarly ideal in nominal value terms, but it still is one of the top 10 countries. From an economic point of view, India is an important partner for China, as wage level is probably even lower than in Southeast Asian countries, which means that it potentially is a preferred outsourcing destination for China. In order for negotiations to start, border issues (in the Tibet region) between the two countries should be successfully settled. The same applies to Nepal between China and India, however from an economic point of view, this country has no particular significance.

Other small developing countries of limited economic importance are: Fiji (Oceania), Mauritius (Indian Ocean), Columbia (South America) and Moldova (Europe).

3. Motives behind Building Bilateral Relations

3.1. China's Negotiation Strategy

Since its accession to the WTO China has engaged in bilateral integrational negotiations. The first negotiations were carried out with two domestic regions: Hong Kong and Macau. From a political point of view, this was a particular situation: different parts of the same country engaged in negotiations with each other. Further agreements were signed with similarly small countries. These negotiations served as a learning process as well: the circle of issues addressed has been enlarged as besides concrete trade-related issues negotiations also concerned the rules of origin, the trade in services and the movement of capital. It is worth noting that China has always taken into consideration its partners' interests, even though these countries, being incomparably smaller than China, all lacked sufficient bargaining power. China does not use uniform template agreements (as opposed to the EU for its Europe Agreements) and seeks to conclude mutually beneficial agreements (win-win strategy). As a result of this pragmatic approach, the content and the scope of the contracts vary in each case. Agreements were signed with the developed countries as a result of such a learning process.

3.2. China's Motives

3.2.1. International and World Economic Factors

From the perspective of the export-oriented Chinese economy, a favourable world economic environment, which accepts China's opening-up policy and is not afraid of China's continuously growing economic power, is of utmost importance. However, in the last two decades, the multilateral rules for international trade (WTO) have barely changed, and the proliferation of bilateral free trade agreements also provoked deterioration in China's world market positions. Yet, this is a dual process. Confining the movement of multinational companies within certain limits as well as China's growing presence in the world economy plays a significant part in the formation of bilateralism, moreover, bilateral efforts of the EU and the US also served as examples for China. China found itself in such a situation as a result of the rule of action-counteraction: it has to react to the strengthening tendency of regional co-operations and also has to engage in the development of bilateral relations. The results are impressive: according to the WTO there are about 300 free trade agreements in force in the world, 5 percent of which China is also involved in. 90 percent of these bilateral (more rarely multilateral) agreements refer to a free trade area of sorts, while the remaining 10 percent is realised in the framework of customs unions (Kruppa, 2016). This non-transparent web of agreements is often referred to as a 'spaghetti bowl' in the literature.

The 1997-98 Asian Economic Crisis challenged the countries of the region which all struggled to keep up their previously high GDP growth rates. First the creation of the AFTA (ASEAN Free Trade Area), then China's strive for integration forced the other countries of the region to join (out of fear of being left out) this process (Kawai & Wignaraja, 2011).

In the early years of the new millennium, the world economy has witnessed the rapid economic growth of the so-called BRIC countries (Brazil, Russia, India and China) and the improvement of their positions in the world market. These countries seek to take part in shaping world economy and politics with the emphasis their economic weight deserves. However, the international institutional framework along with the system of decision-making were formed after World War II in the era of a bipolar world order. This latter collapsed in the early 1990s, but the institutional framework has remained the same. The new unipolar world order (US), and later on the few timid steps in the direction of a multipolar world aimed at creating a new institutional framework and a new system for decision-making on the level of global politics and economy with the participation of the BRIC countries. China's free trade agreements (and the continuing global expansion of Chinese capital) also point in this direction.

3.2.2. Economic Factors

Supporting market access for products of labour-intensive sectors plays a crucial role in China due to the growing number of competitors. Subsidising the exports of high tech products manufactured by foreign-owned companies is also a priority. Through agreements China can secure the increase of its export markets.

It is important to highlight that a significant part of the agreements (projects) were concluded with countries having trade surplus against China. This means that China pays particular attention to these countries in its foreign trade policy, and it also hopes to improve its market positions through signing free trade agreements.

With the help of such agreements China can diversify its imports of raw material and energy carriers. Rapid growth requires the production of a lot of steel and energy (oil and gas). Free trade agreements support the achievement of such objectives.

Signing agreements with developed countries can be motivated by the access to advanced technology and the potential increase of cutting edge technology exports.

Agreements also broaden the horizon for the movement of capital. On the one hand, companies from partner countries tend to install factories in China as trade barriers are removed from exports (not to mention the opportunities a large and expanding market has to offer). On the other hand, agreements bring new investment opportunities for Chinese capital as well: production is outsourced to countries with low wage level, Chinese actors can participate in the exploitation of raw material and energy carriers and take over companies in developed countries, which is the only way for them to obtain their technological innovations.

Supporting the emerging co-operations in production. Kruppa (2016: 26) argues that in Asia co-operations in production will provide the framework for regionalism. I agree with this position. Capital movements in Asia follow the so-called 'flying geese model', which means that a multi-layered supplier and cooperation structure have emerged in the countries concerned (where ownership concentrations are frequent). This model shares common traits with value chains created by the multinationals in developed countries. Both methods are present in China. Chinese foreign trade policy makers have recognised that the expansion of foreign-owned large multinationals can also serve their purposes, therefore China supports them through concluding bilateral free trade agreements with the countries concerned, while it is still trying to channel them (towards partners and from partners to China).

Last but not least, it is crucial for China to be globally approved as a competitive, functional market economy. According to the WTO treaty of accession China will obtain the full market economy status in 2016, it being understood that formal proceeding can still be initiated against China in case of market disruption. Free trade agreements approve China's market economy status (Mingtai, 2009).

3.2.3. Political Motives

It is in fact essential for China to include Chinese diaspora living in the surrounding countries in its economic relations. Most Chinese people living abroad have been members of a so-called 'trading minority' forming middle classes in their respective host countries, which has been liable to trigger envy from the ethnically different local majority. 'Economic nationalism' present in South East Asian countries considered local Chinese populations as foreigners most often loyal to their country of origin, therefore these countries were seeking to impose different restrictions on their economic activities. The positive effect of free trade agreements is the release of these tensions. As to the economic benefits, Chinese products will thus find their way more easily to local Chinese retailers who, in turn, will occasionally act as foreign investors in China (Szép, 2012).

It is also important to underline China's geopolitical interests. It seeks to gain a dominant (but not monopolistic) position in the region. This is why its first few free trade agreements were signed with regional countries which helped China to overtake its regional competitors (Japan, South Korea) and narrow countries' political leeway on other continents.

One of the main objectives is to head off the threat imposed by China. The conclusion of agreements suggest that China is in fact the number one trading power in the region, yet still wants to avoid abusing its economic and negotiating power. China presents itself as the 'benevolent neighbour' suggesting that there is no need to be afraid of the trading giant. (Hilpert, 2014). The basis of the institutional integration theory is that good economic and trade relations are accompanied by correct political relations. In other words, China's aspiration is to improve the political stability of the region and to maintain peaceful relations between the neighbouring countries. "

One of China's most important strategic goals is to enhance regional peace and stability" (Lukács, 2012. p. 72.).

Free trade agreements are also destined to further enhance competition between China and Japan. Although the economic and political rivalry between the two economic powers fosters the enlargement of the integrations, this competition is in fact liable to hinder the development of a formal regional economic structure (Völgyi, 2009, p. 5).

4. Instead of a Conclusion: China and the Integration Process

Free trade agreements have become important parts of China's foreign trade policy. According to Zhang's researches, these agreements have had a significant impact on foreign trade performance, in addition, most of the companies he analysed were aware and took advantage of the fact that FTAs contribute to the promotion of trade. Early Harvest Programs for example have significantly contributed to the expansion of agricultural trade.) In the past few years, China's external trade has expanded significantly.

China is one of the late comers: China has several bilateral agreements, however, China's accession to the WTO is of utmost importance. The changes in the world economy in the 19th century, the increasing role of global value chains and the beginning of the 4th industrial revolution suggest that the answer to the transformation process in the global economy will be an increase in regionalisation trends. The WTO should upgrade or modernise itself to be able to respond to new challenges and to help countries that do not participate in integrations to avoid the negative impacts.
China intends to encourage regional consolidation of peaceful coexistence. Its political and economic objectives are not in conflict. The advances countries however, have been watching China's movements with concern. They attempt to cooperate but without abandoning their own aims. Now in March 2017, the world turns its attention to the US: the economic strategy of the new President may be decisive everywhere in the world (obviously in China as well).

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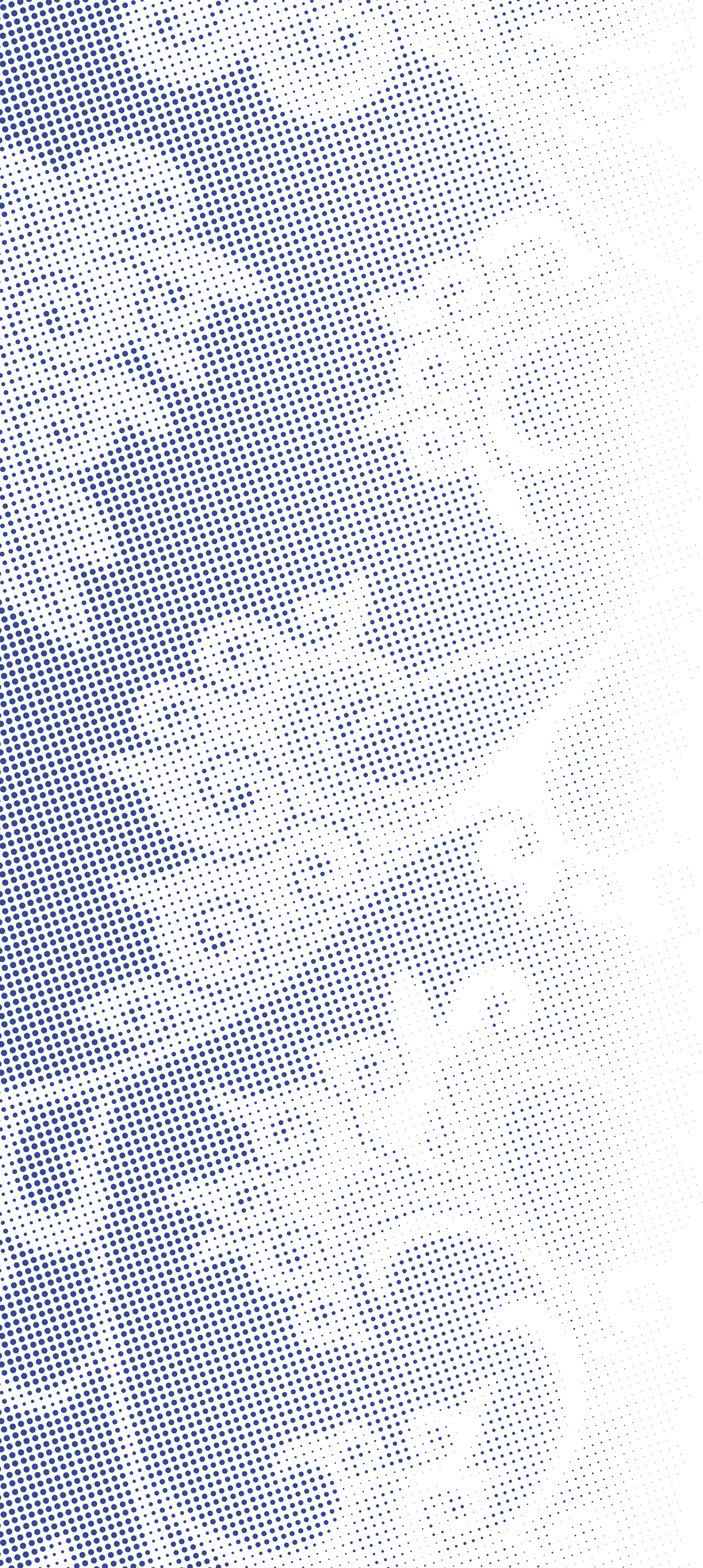


Chinese Investment in the EU and Central and Eastern Europe

Tamás Matura

1. A Short Introduction

The rise of China is one of the most widely researched and discussed topic of our time. Although this sounds like a commonplace nowadays, it is nonetheless true that the rapid domestic economic development of the East Asian giant has arrived at a new milestone. While companies from all around the world have been investing in China enthusiastically in the last thirty years, the development of Chinese outward direct investment on a global scale has inevitably turned the tide.

China has been the greatest beneficiary of the liberal world economy of the last decades. Enormous amount of foreign capital has been and is still boosting the growth of the Chinese gross domestic product (GDP), multinational companies like the Volkswagen Group arrived in the country as early as the mid 1980's to reap the benefits of free trade and cheap, diligent and abundant labour force. Chinese accession to the WTO in 2001 attracted even more foreign enterprises to the People's Republic, while Chinese outward direct investment abroad (ODI) was lagging far behind the amount of inward FDI flows. However, the global financial crisis, economic turmoil in the European Union (EU), overcapacity in China, hunger for resources and the need to invest its surplus capital has changed the trend, probably forever. Today, the Chinese government encourages and supports its (mostly state owned) enterprises to 'go global', to invest abroad, and to acquire assets all over the world. In the first decade of the 21st century Chinese ODI focused mainly on countries and regions rich in natural resources, like Southeast Asia and Africa.

However, the economic and financial crisis of the Western world has brought new opportunities to China. Since the country's further domestic economic development is in need of high technology and know-how, Chinese companies are eager to take over or merge with their European or American peers. The significant decrease in market capitalisation made Western companies quite attractive in the early 2010s, as obtaining them promised access to new technology and new markets, while offering good financial investment opportunities at the same time. Therefore, Chinese attention turned towards Europe and the U.S.. While Washington raised considerable political obstacles due to political concerns, Europeans, including Central European countries, were glad to receive fresh Chinese capital.

Of course, the rapid change of balance between Europe (the largest investor in China) and Beijing has brought some unforeseeable consequences. Political and security concerns have been on the rise in European capital cities and institutions in the recent years, while the sophisticated, regulated and complicated European business environment posed serious challenges to pioneering Chinese companies.

This paper will offer an overview of the development of Chinese ODI and its nature in Europe and in Central Europe in particular. The most important questions to be addressed are as follows: What are the motivations of Chinese investments? Which are the major destination countries and sectors? Does Chinese activity follow a particular pattern, or is it completely random in the EU? Do Chinese companies follow a different strategy in Central and Eastern European countries than in the rest of the EU?

2. Methodology

The aim of this paper is to sum up the recent developments of Chinese investment in Europe and in the CEE region. As the topic is quite new, the countries concerned attract significant political and scientific attention, since more and more decision makers would like to understand the nature and motives of Chinese activity in Europe. As the interrelations between politics and business with China is one of the major concerns, this paper will shed light on some interesting details of this issue as well. The present work processes the already available research papers and other resources while seeks for answers to the above-mentioned questions. In order to present the current status of Chinese ODI in Europe, the paper offers some basic econometrics in form of tables, charts and graphs.

As to the structure of this paper, following the chapters of introduction and methodology, the review of literature and historical perspectives offers insights to what is already known about Chinese investment activity and its political implications. The next chapters explain the details of Chinese investment in Europe and in Central and Eastern Europe in particular, and finally the article will conclude with some recommendations.

It has to be noted here, in this chapter on methodology, that the most general problem of all papers covering Chinese investments is the lack of reliable data resources. Due to diverging statistical standards and methodology, there are significant differences in the data provided by different sources. In some cases, even the scale of data is different, which is a huge handicap if one is to conduct proper scientific research. Following the example of the most relevant papers on the topic, the present work will use data provided by the Ministry of Commerce of the People's Republic of China (MOFCOM), the China Global Investment Tracker of the American Enterprise Institute, the Mercator Institute for Chinese Studies (MERICS) and by Eurostat in some cases.

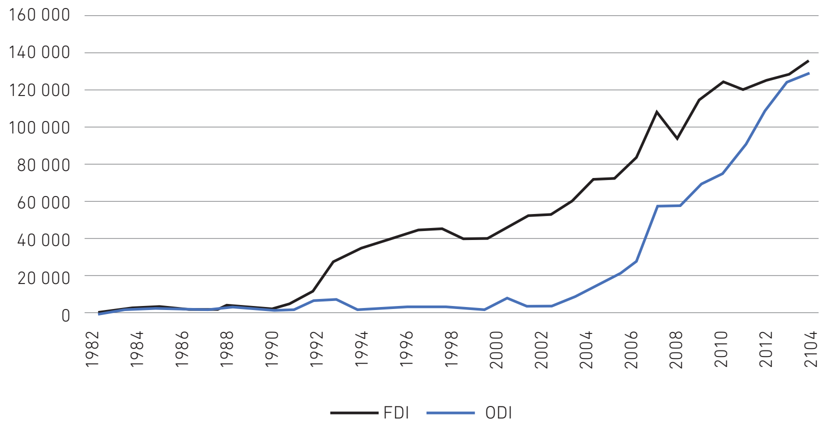
3. Historical Perspectives and the Review of Related Literature

The phenomenal economic development of China has had a major impact on its companies as well. As the economy grew larger and larger, enterprises accumulated more and more capital, and started to seek for new opportunities, sometimes abroad. This development was in line with the general economic strategy of the Chinese state, thus the government actively encouraged its companies to invest abroad, and to turn into multinational companies. In 2005 the Chinese economy accounted for 5 percent of global GDP while only 1.3 percent of global ODI flows originated from China. A few years later, in 2012, China already accounted for 11.6 percent of the global economic output and 6.7 percent of ODI. That is, Chinese firms invested overseas less than their competitors in other countries. (Liu, Q. 2013, p.4.) Chinese companies are catching up quickly. Since 2005, Chinese ODI has been growing at an unprecedented pace, annual outflows have risen at a yearly average rate of 19 percent, reaching USD 115 billion in 2012 and USD 127 billion in 2015. According to most estimates, China has become a net investment exporter for the first time in history in 2016, as outward capital flow exceeds inward flow of capital. (Diagram 1)

The composition of the type of companies investing abroad has recently been changing as well. As Chinese enterprises are getting bigger and the domestic economic growth slows down, it is a strategic decision or necessity to expand their activity abroad in order to get a competitive edge over their domestic competitors. While manly huge state-owned enterprises started international ventures during the initial period of the 'go global' strategy, today non-state firms have increasingly been activity participating in outward investment, and the share of state-owned enterprises (SOEs) is falling. (Alon – Wang et al, 2014, p.11.)

Diagram 1

Flow df Chinese FDI and ODI



Source: UNCTAD Stat

The first driving force behind Chinese ODI was the hunger for natural resources. Thus, Chinese companies invested mostly in developing, resource-rich countries in Southeast Asia or Africa. By the early 2010's the situation has changed in China, therefore nowadays firms are mostly seeking for technology, know-how, brands and market share.

4. The Strategy of 'Going Global'

The strategy of 'going global' *(Zǒuchūqū Zhànlüè)* was introduced by the Chinese government in 1999. The first years after the initiation of this new approach were less successful, with some significant failures. The second half of the 2000s witnessed a tremendous increase in Chinese ODI outflows, shaken only temporarily by the global financial crisis. Over the past decades, the Chinese economy has been relying mostly on growing volumes of exports and major infrastructure investments, until the outbreak of the global crisis. Structural changes in the world economy have drawn the Chinese government's attention to the fact that relying upon the export of low value-added manufactured goods or building more infrastructure cannot ensure the sustainable growth of the Chinese economy anymore. Instead, Chinese firms have to move up on the value chain of the global manufacturing sector and generate more and more wealth domestically.

The economic model of China produced, in the previous decades, huge foreign exchange reserves, and the financial crisis in Europe offered a unique opportunity to utilise that capital to acquire financially distressed European firms equipped with the industrial and commercial technology and know-how. The 'going global' strategy exposes companies to mature markets, and it will force them to learn management skills and further intangible assets abundant in developed countries but scarce in China. Another reason behind the strategy was to relieve political pressure on renminbi exchange rates with the world, while it indeed turned out to be a better investment strategy than buying government bonds. The latter option was too risky during the years of the eurozone crisis, while the opportunity to acquire European companies at low market capitalisation was tempting. (Yu, 2012, pp. 34-35.)

Filippov and Saebi (2008) describe three main motives behind China's investment strategy. First, macroeconomic reasons (like the enormous amount of foreign exchange reserves[1]) make investing abroad inevitable for China. Second, business motives also play an important role, as major Chinese companies look for international opportunities to expand, gain experience, and withstand competition both at home and abroad. As to the third important motive, it has in fact a political tint: China intends to expand its political influence to the globe. The authors state that Europe has to face the perils of the strong political influence of the Chinese government mediated by its state-owned and even private companies. As a consequence, Chinese investment potentially increases the political influence of Beijing in the European Union. (Filippov and Saebi, 2008, pp. 27-29.)

Quan Li and Guoyong Liang (2012) argue in their work on the correlation between Chinese outbound foreign direct investment and political relations that international relations and foreign policy do play an important role in Chinese ODI. The authors identified the reasons for and the mechanisms through which China's political relations with potential host countries significantly influence firm investment decisions. Based on their conclusions, Chinese outward direct investment is more likely to rush to countries with which the Chinese government has a good political relationship, in the hope of better protection and treatment of their investments. (Li and Liang, 2012, pp. 20-21.)

1 Since the national currency of China (RMB) used to be non-convertible, and is semi-convertible today, net FDI inflow, net exports and other financial inflow into the country has accumulated an enormous foreign exchange reserve in the hands of the state. The State Administration of Foreign Exchange (SAFE) manages the reserves of the country, peaking at USD 4trillion in 2014. Before the global financial crisis, China invested most of its reserves in foreign government bonds (mostly in the US) and other safe instruments. The government decided however to take advantage of the economic meltdown in the West and it has been encouraging its companies to take over their Western competitors with the financial support of the immense foreign exchange reserves.

The picture drawn by Brown and Wood is even more concerning in their book on Chinese ODI. They conclude that the Communist Party of China and thus the government itself of the People's Republic consider making investments abroad as part of a national strategy, and not something motivated by economic or commercial considerations. Chinese companies represent the interests of the party and the state through their global investment patterns as well, and the global expansion of Chinese investments is also motivated by strategic considerations. (Brown and Wood, 2009.)

5. Chinese Activity and Investment in Europe and Central and Eastern Europe

5.1. China and the Major EU Countries

The recent history of Chinese ODI in the European Union can be divided into three main stages: pre-crisis stage, crisis stage and post-crisis stage. The first stage started in 2001 and lasted until 2008. During this period, China joined the World Trade Organisation, encouraged its companies to 'go global', but most of its activities focused on countries rich in natural resources and raw materials and Europe was not eager either to attract Chinese capital. However, the period of the financial crisis (2009-2012) offered new opportunities to China, thus Beijing actively encouraged its companies to take advantage of the European crisis and acquire undervalued companies, while most European governments happily received Chinese money. The post-crisis period (since 2013) is still dynamic in terms of inflow from China, but investors from the Middle Kingdom seem to be more sophisticated and less opportunistic. They have learnt the lesson from EU regulations, business environment and standards of the previous periods. Chinese companies have been increasingly turning towards foreign markets since 2013 to diversify their investments and increase their market share. Europe is an ideal destination since European companies possess valuable intangible assets (technology, know-how, and brand names), which Chinese companies lack. These assets will help Chinese companies at home and abroad to move up the value chain and please their customers back in China who prefer European brands. Another reason for the vivid Chinese interest in investing is the relative ease (especially compared to the US) to purchase European companies and markets. Finally, China enjoys a good bilateral relationship with the EU and the proposed bilateral investment agreement may secure even better market access for Chinese companies in the future. Although compared to China European markets offer a lower rate of return, it still is considered to be a stable, low-risk form of investment (Jia, 2015, pp. 3-5.)

The opportunity provided by the financial crises multiplied China's annual ODI flow to the EU between 2009 to 2011 by about 30 times. By the end of 2011 it has amounted to EUR 3.19 billion and its stock has reached EUR15.03 billion. What is remarkable is that according to more recent data from China's Ministry of Commerce it seems that the annual flows of China's ODI to the EU have already surpassed that of the EU to China. By the end of 2012, China's OFDI stock in the EU has amounted to EUR 24.4 billion (EUSME, 2014, p.1.)

Providing clear evidence of the sustained Chinese interest, new data show that the stock of Chinese investment may have reached EUR 100 billion by the end of 2016. (Hanemann – Huotari, 2016, p.7.)

Recent changes in the Chinese attitude and approach can be summarised in the followings. Private Chinese firms have taken over the initiative from state owned enterprises in the majority of the acquisitions in terms of volume. The UK, Germany and France are the main preferred countries for the completion of Chinese M&As, especially for deals in high-tech and knowledge-intensive sectors. Mergers and acquisitions are the main forms of entry for Chinese investment in Europe, and the trend is likely to continue, since Chinese firms tend to target sectors in which European companies have world-class operational, managerial and innovation expertise. Investment by wealthy Chinese individuals or families is a new phenomenon, explained both by the increase of a wealthy middle class in China and the consequences of the recent crackdown on corruption by the Chinese government. Europe is a perfect place for Chinese companies to invest as these investments cannot be controlled by the party or the state. (Table 1)

Chinese investors have followed the example of other, traditional foreign investors in Europe by putting most of their investments in the wealthiest and largest European economies. Germany, the UK, and France have received EUR 4-8bn annually over the last five years and they continued to be major targets in 2015. The major development of the past two years, however, is the rapid increase of Chinese ODI on the periphery of Europe. In 2015 South European economies absorbed almost half of all Chinese investment in the EU. High-profile deals (the acquisition of Pirelli, Atletico Madrid, Banco Espirito Santo's investment banking business) granted China the position of a significant investor in those economies. Investments in the Benelux countries have also significantly increased in the past two years and pending projects could further increase Chinese presence in Eastern Europe if they materialize. (Hanemann – Huotari, 2016, p. 6.)

Table 1
Stock of Chinese Investment in the European Union (2015)

#	country	stock (EUR million)	#	country	stock (EUR million)
1.	United Kingdom	23.633	15.	Greece	840
2.	Germany	18.817	16.	Czech Republic	569
3.	Italy	12.839	17.	Austria	551
4.	France	11.458	18.	Luxembourg	499
5.	Finland	6.854	19.	Bulgaria	337
6.	Portugal	5.726	20.	Denmark	209
7.	Netherlands	5.598	21.	Malta	70
8.	Spain	3.015	22.	Slovakia	49
9.	Ireland	2.723	23.	Cyprus	45
10.	Hungary	2.051	24.	Lithuania	33
11.	Belgium	1.808	25.	Estonia	23
12.	Sweden	1.592	26.	Slovenia	8
13.	Poland	936	27.	Croatia	4
14.	Romania	889	28.	Latvia	3

Source: Mercator Institute for Chinese Studies, 2016

From a Central and Eastern European point of view, the role of Germany in the Chinese investment activities is a crucial one, as major CEE countries depend on the performance of the German economy. Europe's largest economy is the second largest recipient of Chinese ODI in Europe, with investments in the period between 2000 and 2016 adding up to €18.9 billion. Germany's advanced manufacturing capabilities are still the major driving force for Chinese investors with automotive and industrial equipment accounting for more than 65 percent of total Chinese investment. The industry mix has recently incorporated IT equipment, finance and business services, as well as consumer products gathering interest. Most deals in Germany were small and medium sized takeovers, with state-owned companies. (Hanemann – Huotari, 2017, p. 6.)

It has to be added however that the German government has developed serious concerns about the technology targeted by Chinese takeovers. For instance, the potential Chinese acquisition of KUKA AG and its highly advanced robotic technology has triggered a serious political upheaval in Berlin in 2016.

5.2. Central and Eastern Europe and the 16+1 Cooperation

Friendship is to be established first to facilitate good business relations later, at least according to the Chinese way of thinking. Somewhat suspicious Western diplomats have been asking the following questions at least since the summit in Warsaw in 2012:

“Why is Central Europe so important to Beijing now, what is so special about these sixteen countries? Does China want to divide and rule the EU through the 16+1 mechanism?” China has built splendid political relations with many countries and regions all around the world where it hoped to find potential trade and investment opportunities. Having already developed its global presence in Africa, Asia or Latin America, China had to find new partners. The crisis of the European Union and the resulting financial vacuum revealed potential opportunities in the CEE region. Even though these opportunities are modest compared to the usual Chinese appetite, Beijing is eager to seize every opportunity to find business projects for the overcapacity of its companies and its abundant financial assets.

When Beijing introduced the outlines of the cooperation between the Middle Kingdom and its sixteen Central and Eastern European partners in 2011-2012, most observers believed that China already had a well prepared and detailed plan somewhere in the offices of its Ministry of Foreign Affairs. Since this strategic document has never been published or even talked about, some experts and politicians developed concerns about the true intentions of China. At the same time CEE countries have been trying hard to figure out what Beijing wanted or needed. Only a few have realised that the Chinese way of thinking and communication was different from the Western style: Beijing follows the traditional East Asian inductive way of thinking, while its European partners try to understand the Chinese side through their deductive traditions.[2] Consequently, countries with different traditions are suspicious about China’s intentions, since they think there might be a hidden agenda behind the curtain. Through the 16+1 mechanism it has become clear that a proactive attitude should be adopted by the participating countries to shape the project in cooperation with China. There is no secret plan, China rather fosters the organic development of this cooperation.

According to the experiences of the last six years China intends to keep its activities in the spheres of economic and business cooperation with the CEE region and to avoid any international political problems. The regular invitation of the officials of the European External Action Service to the 16+1 summits and other event reduces suspicion about the true intentions of the cooperation. Based on the experiences of the

2 East Asian inductive thinking means that projects are built in an evolutionary, step-by-step approach, where the final aim is a bit vague, and objectives are set in a bottom-up process. On the contrary, the Western deductive mindset creates the strategic level plan or blueprint first, then starts to figure out the details in a top-down way. This difference can easily lead to misunderstandings, as in the case of the 16+1 project, where EU institutions were suspicious about the true intentions of Beijing, since due to the lack of a transparent strategy or plan many developed baseless fears of a secret Chinese strategy.

last five years, there are no signs of strategic level political requests from the Chinese side, which could be considered as an attempt aiming at the weakening of the EU's common policies or integrity. Furthermore, as a response to initial accusations, now both Beijing and its Central and Eastern European partners emphasise that the 16+1 is fundamentally part of general EU-China relations.

Besides political issues, there are still numerous structural problems and contradictions hindering the progress of the 16+1[3]:

5.2.1. Size and Complexity

When China created the 16+1 cooperation, it invited all countries between the traditional 'West' and 'East' from the Baltic to the Balkans, with the exception of Belarus, Ukraine, Kosovo and Moldova. Meanwhile, there are some questions with regard to the effectiveness of such a broad and comprehensive cooperation of seventeen countries very different is their size as well as their economic and political status. According to personal talks with researchers, the Chinese side is aware of the complexity of the CEE region, therefore evaluation of possible sub-regional forums, like a China-V4 dialogue, was initially supported by the Visegrad countries. However, it seems that the Chinese Ministry of Foreign Affairs does not support such ideas. The MFA regards the 16+1 mostly as a transaction cost reducing tool, which gathers sixteen national leaders at the same time. The sub-regional level would erode this feature of the China-CEE cooperation, therefore, Beijing is unlikely to support a V4-China forum. There is also little chance of working out common V4 standpoints vis-à-vis China, since the Czech Republic, Hungary, Poland and Slovakia are mostly competing with each other for Beijing's attention.

5.2.2. Trade and Investment Issues

Although capital- and trade-seeking CEE countries look at China as a potential source of foreign direct investment and trade opportunities, there are serious doubts about their governments' ability to influence bilateral economic cooperation between their respective nations and China. In the field of FDI issues there is a fundamental contradiction between Chinese and Central European intentions. While China is mostly looking for infrastructure investment opportunities (preferably through governmental

3 The following points are partially based on the corresponding chapter of *The Visegrad countries' Political Relations with China: Goals, results and prospects* (Richard Q. Turcsányi – Tamás Matura – Rudolf Fürst In: Á. Szunomár (ed.): Chinese investments and financial engagement in Visegrad countries: myth or reality? Budapest: Institute of World Economics, 2014, 178 pages (ISBN 978-963-301-615-2)

public procurements), most CEE countries are keen to attract greenfield investments in order to create jobs and industrial production. However, according to the dataset of China Global Investment Tracker of the American Enterprise Institute, China has barely set up any newly established facilities in the region. Chinese companies rather pursued mergers and acquisitions (M&A) or infrastructure building opportunities. Central European EU member states can apply for non-refundable financial support for infrastructure development, while the regulations of potential Chinese credit lines are not in accordance with EU procurement law. Therefore, Chinese loans are not attractive, while any attempts to pay off Chinese construction companies from European funds might likely provoke political turbulences. Both sides are looking for something different, which is a fundamental problem, with the exception of non-EU member states on the Balkans, where Chinese investment into infrastructure has been more successful.

When it comes to merchandize trade issues, the role to be played by CEE governments seems to be even more modest. In the case of the Czech Republic, Hungary and Slovakia approximately 90 percent[4] of exports to China is produced by foreign-owned multinational companies. It is clear that governments in Budapest, Bratislava or Prague cannot really influence such trade relations, no matter how good (or bad) their relations are with Beijing. Meanwhile SMEs in Central Europe are usually too weak to facilitate their own business relations with their Chinese counterparts. This is also a serious problem to be addressed.

The total bilateral trade volume between China and the 16 CEE countries amounted to $74.8 billion in 2014, which was 11.8 percent of total EU-China trade (UNCTAD Stat). Since the trade dependence of CEE countries on EU markets is between 60 to 90 percent, it was logical to seek alternative trade opportunities amid the raging European financial and economic crisis. Although most CEE countries have to face a major trade imbalance with China, in most cases the deficit itself is not a real problem, since the majority of imports from the PRC represent spare parts, accessories and other inputs for CEE industrial production. Therefore, the majority of imported Chinese goods are re-exported to other EU countries, mostly in Western Europe, as parts of high-tech products manufactured or assembled in CEE countries. In the meantime, the story of exports to China is less satisfying, since indigenous CEE products can rarely find their way to China due to the lack of quantity or proper financial background in most cases. Another important fact is that the overwhelming majority of CEE exports to China are produced by multinational companies located in the countries of the region. In case

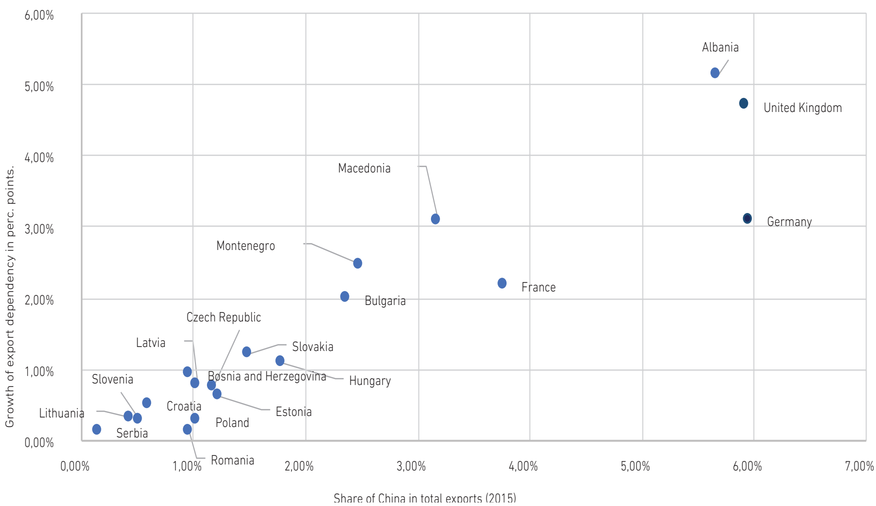
4 Based on estimates of local experts and non-public data of the Hungarian Central Statistical Office.

of Hungary or Slovakia the share of MNCs reaches 93-99 percent of their exports to China, but some two-thirds of Polish exports are falling in the same category.

The following two graphs offer a comparative analysis of the relatively low importance of trade relations between China and individual CEE countries. Compared to major, Western EU member states, CEE countries have a low export dependency[5] on China, and even the growth of this dependency has been very modest in the recent years. Data on the strength of political relations is offered by Liu Zuikui's paper entitled 'The Analysis of China's Investment in V4 in: Current Trends and Perspectives in Development of China-V4 Trade and Investment' (see below).

Diagram 2

Growth of export dependency between 2004 and 2015 and the share of China in total exports in 2015



Source: Own calculations based on Liu (2014) and Unctad Stat

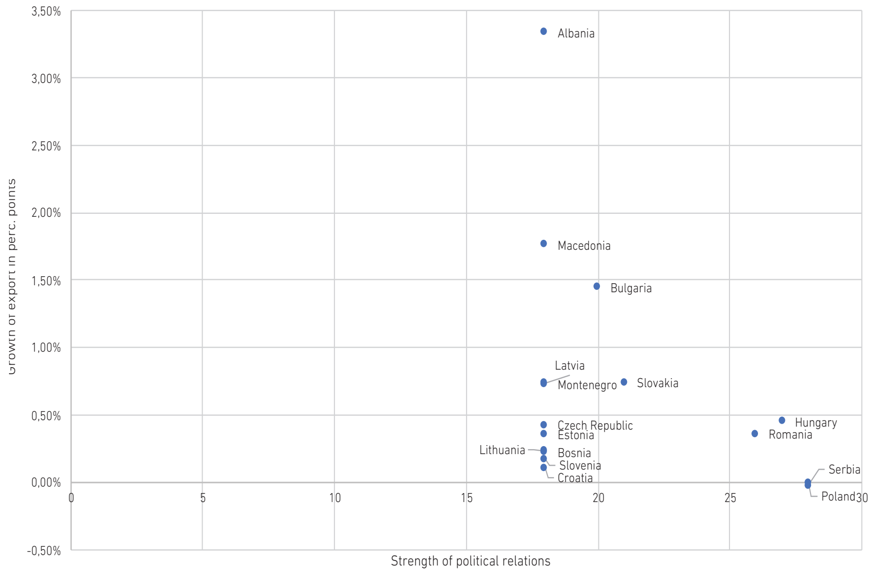
What is even more remarkable is the lack of correlation (or actually the negative correlation) between the quality of political relations and the development of exports to China from individual CEE countries. The significance of this phenomenon stems

5 Export dependency is calculated as the share of exports to China in total exports of the respective countries.

from its surprising contrast both with typical stereotypes (i.e. better political relations with China leads to more trade) and with investment relations, where the quality of political relations indeed does matter.

Diagram 3

Strength of political relations (2014)
vs. Change of export dependency vis-à-vis China (2009/2014)



Source: Own calculations based on UNCTAD Stat and Liu, Z. (2014)

5.2.3. Structural Contradictions

Considering different fields of cooperation[6] between China and the 16 CEE countries, it is noticeable that the two sides aim to work together in spheres which are mostly regulated by Brussels. Thus, the eleven EU member states of the 16+1 cooperation have to walk on a thin line between China and the EU. The rules of the investment, trade or financial environment are generally set by EU level policies, even when it comes to issues like tourism (e.g. Schengen visa). Consequently, EU member states of

6 For further information see the different guidelines published following the summits (Warsaw, Bucharest, Belgrade, Suzhou, Riga)

the region cannot do too much to please China. Of course, the business community is the one which may facilitate relations, but then the actual role of the 16+1 mechanism itself is questionable. Meanwhile areas where member states enjoy full sovereignty, like education or culture, are being developed mostly on a bilateral level, and not in the framework of the 16+1.

The above-mentioned structural contradictions boil down to the surprisingly ironic conclusion that non-EU countries where EU regulations and standards do not apply (or are weaker) are more able to cooperate with Beijing than EU members of the region, while the latter have done everything to position themselves as a hub, centre or bridge for China in the European Union. Numerous successful deals between China and Western Balkan countries offer a substantial evidence to this assumption (see below).

When it comes to China, history does matter, thus some important remarks are to be made on the historical context of the China–Central and Eastern Europe relations. First of all, CEE countries have never invaded the Middle Kingdom in the last centuries, and this is something our Chinese partners mention regularly. Second, CEE countries were the first to establish diplomatic relations with the newly proclaimed People's Republic of China as early as October 1949. This fact still matters politically to Beijing. Bilateral relations were deeply influenced by the Sino-Soviet split during the worst periods of the Cold War, and after the collapse of communism in Europe countries of the region focused efforts on their NATO and EU accession processes. Consequently, relations to China were not prioritised until the very first decade of the 21st century. The Hungarian government was among the first to 'rediscover' China right after Budapest successfully concluded its EU accession process in 2003. The then Prime Minister Peter Medgyessy paid an official visit to Beijing in August 2003, and all Hungarian prime ministers have visited Beijing over the course of the past decade, most of them more than once. In the meantime, other countries of the CEE region have tried their best to boost economic relations with China as well, but it was the European financial crisis which contributed the most to the changes in European attitudes vis-à-vis China.

The major economic downturn, when traditional foreign direct investment and financial resources dried up in Europe has given a new impetus to China-CEE relations. Financially less stable EU member states were forced to find new business opportunities both in Central and Southern Europe. At the very same time China had to tackle with the oversupply of cheap capital and industrial overcapacity. The need in Europe and the will in China seemed to create opportunities benefiting both sides. As an effort to create a new momentum for bilateral relations, the Hungarian government was eager to host the very first meeting of the Central and Eastern European Countries and China in Budapest in 2011. The next meeting, or the first summit for the 16+1 prime ministers (16 from the CEE region and their Chinese counterpart) was organised in Warsaw as a clear sign of mutual interest in 2012. As a next milestone of the development of cooperation, the Ministry of Foreign Affairs of the PRC established the Secretariat for China-CEE Cooperation in September 2012. The third meeting in Bucharest (2013), the fourth in Belgrade (2014), the fifth in Suzhou (2015) and the sixth in Riga (2016) have all proved the sustainability of the project, while the seventh meeting will take place in Budapest in 2017.

As of today, the 16+1 cooperation is not an institution, but an intergovernmental mechanism, with the main aim to reduce the transaction costs of interactions between China and the CEE region. Technically, the 16+1 summits are forums where the Central and Eastern European countries involved (11 of which are already members of the EU) enjoy the opportunity to meet the Chinese premier on an annual, regular basis. Obviously enough, without this mechanism, chances for minor regional countries to have bilateral talks with the Chinese PM would be minimal. Even German, French and British leaders are eager to travel to Beijing on a regular basis to sign major business agreements, thus it is understandable that CEE leaders would also seize the opportunity to make at least some minor deals. From China's point of view, it is also more convenient and attractive to gain access to the governments of 120 million people at the same time and place instead of conducting bilateral talks one by one.

Although there have been political considerations both in certain CEE capitals and in the EU, the basic purpose of 16+1 cooperation is economic in nature. Debates regarding human rights and democracy used to be thorny issues in Czech-Chinese and Polish-Chinese relations, however, these have mostly faded away, like in other Western European capitals. It is more convenient for governments to leave these issues to the European Parliament and other EU level institutions in order to ease bilateral relations with China. Trade, investment and business are what really matter today, at least according to most CEE politicians.

When it comes to investment relations, the picture is even more opaque as official statistical data are inaccurate and contradicting. For instance, the stock of Chinese FDI in Hungary amounts to around USD 600 million according to the European and Chinese statistical bureaus, while the real number exceeds USD 2 billion and is probably closer to USD 3 billion. The real problem, however, stems from the divergent economic interests of China and the CEE countries. The region would like to mostly attract greenfield foreign direct investments in order to create new jobs and boost production and tax incomes (Kaczmarski and Jakóbowski, 2015). At the same time the Chinese are mostly interested in mergers,and acquisitions and in public procurement tender opportunities for infrastructure construction. Even though Beijing is willing to provide financial solutions for infrastructure development in the region, China would rather offer loans and credit lines instead of non-refundable financial sources as provided by the European Union. Nevertheless, if CEE governments decided to finance Chinese construction using European funds, it would surely spark heavy criticism.

5.2.4. Political Aspects

Chinese investment activity in Central and Eastern Europe is a new phenomenon, and it constitutes a relatively small share of China's total FDI in the European Union. The rise of inflows of Chinese ODI into the region is however to be expected due to recent political and economic developments between China and CEE countries, especially Hungary and Poland, or more recently the Czech Republic. (Szumomár & Biedermann, 2014)

Liu Zuokui, the Director of the Central and Eastern European Center of the Chinese Academy of Social Sciences offers a unique insight into the Chinese perceptions of political relations with CEE nations. In his fundamental paper, Liu introduced a ranking system to evaluate the quality of relations between China and the CEE countries. Liu's bilateral relationship indicator includes partnership treaties, top-leader visits, mutual public favourability, investment and trade treaties, etc. The maximum level of this indicator is at 30 points, thus Poland (28), Hungary (27) and Romania (26) have the best bilateral (political) relations with China, while Slovakia (21) is lagging behind, and the Czech Republic (18) sits at the bottom of the ranking (Liu, 2014, p.29.).

Liu's paper also offers insight into the motives for Chinese investment in CEE countries. In his opinion the Greek sovereign debt crisis triggered economic problems in the EU, and offered a "window of opportunity" to Chinese companies. However, as soon as the economic situation starts to improve in the EU, CEE countries will return eventually to their traditional Western European partners, and thus investment opportunities for countries like China will diminish. Liu emphasizes the economic and geographic advantages of CEE members of the EU, and that better political relations with China also mean better investment opportunities for CEE countries. However it is also true the other way around, since tensions in Czech-Chinese bilateral relations have had a deteriorating effect on Chinese capital flows into the Czech Republic. He draws attention to the already mentioned detail that EU membership is not necessarily attractive for Chinese companies, as it means more regulations and less flexibility. Non-EU member countries may provide more opportunities and are more accessible countries for investment.

It is important to note that according to Liu's analysis, China does not invest in all CEE countries indiscriminately, as Chinese companies pay more attention to countries with better investment environment, more balanced composite indicators or with geographical advantages. EU members like Hungary and Poland tend to attract Chinese investment with the promise of further expansion opportunities to bigger EU markets. Hungary has been the first country to attract Chinese institutions to the region, like the Central European headquarters of the Bank of China or the Chinese-Hungarian Bilingual School.

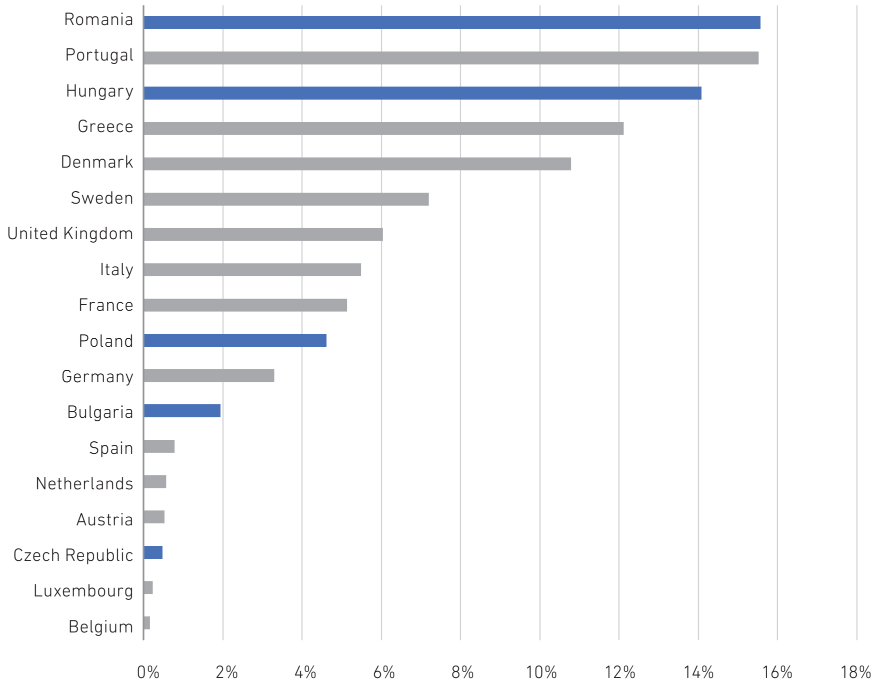
The second important paper on the quality of political relations between China and individual CEE countries is the paper of Chen Xin and Yang Chengyu, experts of the Institute of European Studies of the Chinese Academy of Social Sciences. Chen and Yang apply econometric models to calculate the indicators in the Bilateral Relationship module, while their indicators are based on the numerical value distribution from '0' (worst) to '10' (best). The indicator of 'Political cooperation' is based on four indexes: partnership; high level relationship; diplomatic visit; joint statements. Even though their methodology is different from Liu Zuokui's approach, the results and the priority order of countries in the field of political relations with Beijing is mostly the same: Poland (10), Hungary (9.83), Serbia (9.81), Croatia (5.68), Albania (5.47), Czech Republic (5.46), Romania (5.23), Macedonia (3.74), Bulgaria (3.08), Bosnia and Herzegovina (2.2.), Slovakia (1.9), Lithuania (1.58), Estonia (1.54), Montenegro (0.93), Slovenia (0.79) and Latvia (0) (Chen & Yang, 2016).

5.2.5. Investment and politics

CEE countries have only received a small fraction of all Chinese investment in the European Union. Major EU member states have received the bulk of FDI originating from China. However, when it comes to the share of Chinese investment as a share of total FDI flow in the recent years, Romania, Portugal and Hungary have reached an exceptionally high level, followed by Greece. Of course, it has to be taken into account that all the above-mentioned countries are relatively small, thus one single major Chinese investment may have significantly influenced their respective figures. Hungary is an excellent example of it, since the acquisition of the chemical company BorsodChem by Wanhua Industrial Group represents approximately two-thirds of all Chinese investment in the country.

Diagram 4

Share of China in FDI inflows (2010-2015)

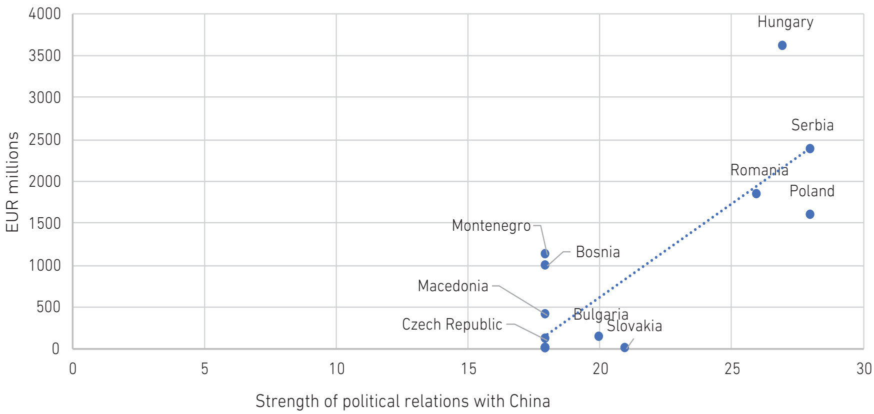


Source: own calculations based on UNCTAD Stat and American Enterprise Foundation

In order to incorporate all possible Chinese investments into the analysis, the present work is based on the American Enterprise Foundation's China Global Investment Tracker (formerly known as Heritage Foundation) datasheet (Heritage, 2015). The AEF statistical database includes both settled transactions and contracts. Based on their data the following chart compares Chinese investment stocks in CEE countries with their political relations with Beijing. Unlike in the case of trade relations, the picture here is clear: there is a strong and positive statistically significant correlation (r=0.83) between the two variables.

Diagram 5

Chinese investment in CEE countries vs. Strength of political relationswith China



Source: Own calculations based on Heritage (2015) and Liu, Z. (2014)

That is, countries with stronger political relations have higher stocks of Chinese investment. The result is in line with the conclusions of Quan Li and Guoyong Liang that Chinese investment is more likely to flow to countries with which the Chinese government has better political relations, in the hope of better treatment and protection of their investments (Li & Liang, 2012). It is also in accordance with Liu Zuokui's paper stating that better political relations with China leads to better investment opportunities for CEE countries (Liu, 2014). However, there is one important detail which makes the picture less obvious: if timing is also taken into account, then Hungary appears to be a special case. Even though Budapest has some of the best political relations with Beijing and hosts by far the highest level of Chinese investment in the region, Hungary has not received any new Chinese investors since the launch of its new China Policy and the establishment of the 16+1 cooperation. Thus, there may be other variables as well, which do influence the flow and the direction of Chinese investments. If one considers the pan-European distribution of Chinese investments, overall business environment and the competitiveness of host countries seem to be two important factors of investment decisions of Chinese companies. On the CEE level the answer is less obvious, since the relatively low number of deals so far may distort the picture to some extent, and thus one might conclude that political relations contribute to the initial phase of investment, but regular laws and rules of the business prevail on the long run.

It has to be underlined, however, that results tell nothing about the causality between the two factors of the quality of political relations with Beijing on the one hand and the level of FDI on the other. The level of investment stocks can be either the cause or the consequence of the quality of political relations. Of course, reality might be somewhere in between. Among CEE countries Romania and Hungary received, in relative terms, the most investment from China based on its share of the total FDI inflow in the two countries between 2010 and 2013. (Let us recall that Hungary attracted no new Chinese investors after 2010. The inflow of Chinese FDI after 2010 is simply the prolonged result of investment decisions made by companies present in the country prior to 2010.) Even though Chinese investment did not contribute to a great extent to the FDI inflow of the rest of the CEE countries, it played an important role in Portugal, Greece, Sweden, France and the United Kingdom as well.

Regarding the form of ownership, 60 percent of capital was invested by private firms (like Wanhua Industrial Group, Huawei Technology, Great Wall Motor and China Ming Yang Wing Power Group), while the remaining 40 percent is attributable to state-owned enterprises (like Guangxi Liu Gong Machinery, Huadian, Sinomach, China Power Investment and China Energy Engineering).

In order to double-check the importance of investment relations, I verified the correlations between investment stocks in individual CEE countries and the three other CASS ranking factors. The economic environment has a weak but positive effect (r= 0.15), the (domestic) political environment has a weak, statistically insignificant and negative effect (r= -0.13), while social environment has a weak and positive (r=0.10) correlation with investment stocks, all statistically insignificant, which supports the assumption that bilateral political relations have had by far the greatest impact on China-CEE investment relations.

To conclude, better political relations with China do mean better investment-attracting ability for CEE countries, at least in the initial phase of investment relations. It is also remarkable that the size of the host economy seems to be less relevant than other factors so far. Poland, the largest economy in the region, has been able to attract much less Chinese investment than Hungary, while Belgrade and Bucharest have also been more successful than Warsaw. The result is also in line with Liu Zuokui's statement regarding the impact of unfavourable Prague-Beijing political relations, explaining the low level of Chinese investment in the Czech Republic.

6. Conclusion and Recommendations

Europe has to accommodate itself to the age of global Chinese investment. The tide is already turning: after decades of intensive European activity in China now companies of the East penetrate Western markets. Generally speaking, competition is good for both sides, Chinese FDI may contribute to the general investment level, to R&D spending and may create new links to global value chains. However, to grab these opportunities, the EU and its member states should increase their competitiveness, and have to prepare themselves to China specific issues (more research, more staff is needed).

There are many concerns as well. The major issue is the lack of reciprocity between the two sides. While Chinese companies can easily act on the soil of the EU, European companies have to face many official and unofficial obstacles in China. Fair competition is still far from becoming a reality, as the Chinese state offers subsidies and other kinds of support to its companies. The EU should be strict on rules of level playing field, and a bilateral investment treaty may help to achieve European goals.

Compared to the more developed Western members of the European Union, Central and Eastern European states are more eager to attract investment from China. However, due to the huge differences in size and power, CEE countries have to be very cautious when engaging with China. The strong correlation between the quality of political relations and the stock of investment may push leaders in the CEE countries to offer political favours in exchange of economic gains. Such a trend may threaten EU level China policies and the general integrity of the Union. Ironically, the fundamental interest of CEE countries is to have a strong EU being able to represent its members when dealing with Beijing. Still, short-sighted and selfish national interests may prevail over the strategic interests of the EU. A race to the bottom approach followed by CEE countries would only benefit China on the long run, thus stronger integrity of member states in CEE and on the EU level as well is highly recommended.

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Trade Relations Between the EU and China and What History Tells Us about Them

Ambrus Gábor Szentesi

1. A Brief History of the Relations

The European Economic Community and the People's Republic of China established diplomatic ties in 1975 on the waves of a wide Western diplomatic recognition of the Beijing-regime. Some of the European multinational companies – such as the Volkswagen – were among the first foreign enterprises to invest in the Chinese economy under reform. In 1985 the two sides concluded the Trade and Economic Cooperation Agreement (TECA) as the main legal instrument to regulate bilateral trade and economic activities. (Men, Balducci 2010) Trade ties gradually improved as China was stepping up with its Reform and Opening up policies, then took an even steeper uphill course since the country's accession to the WTO in 2001. The scope of the ties widened to a vast level through the 2000s, the two sides are now engaged in 59 ministerial and sectoral level dialogues (ESPO) ranging from environmental issues through trade relations to aerospace co-operations. The annually held EU-China dialogue secures a constant platform for extensive exchanges.

The two sides think of each other in an increasingly strategic manner. China's official stance towards developing its relationship with the EU is stated in 2014 document covering 10 major areas. (Ministry of Foreign Affairs of the People's Republic of China 2014) The same year Chinese President Xi Jinping delivered a speech to the EU describing the interactions between the two sides as exchanges between "two civilizations", which in imperial China would have been seen as a clearly strong recognition of culturally equal footing of the relations. The EU first moved towards adopting an Asia-strategy as early as 1994 with the Commission's communication to the European Council and to the European Parliament on the new strategy towards Asia. With China's rise as a global economic powerhouse, the EU realized the necessity of a distinct China-strategy as well. In 2013 it adopted the EU-China 2020 Strategic Agenda (European External Action Service 2013), in which trade and investment issues appear in leading position. In 2016 the Commission along with the Council published the bloc's new strategic document in regards to the relations to China (European Commission 2016; European Council 2016), that echoes a not any more so rosy picture of the relations, first among all, trade and investment relations.

2. Problems and Frictions, Complexity, Purpose

The legal framework of the trade relations between the two sides is determined by the European Union's common trade policy, China's trade policies and practices, as well as the World Trade Organization, of which both entities are members. The importance of the legal frameworks in how the two treat each other and settle their trade disputes cannot be overstated, since (1) the EU and China are two of the world's largest traders, and (2) they are the second and first most important trade partners to each other respectively.

Although bilateral economic relations prosper on the surface, internal economic troubles – inter alia – on both sides have increasingly serious effects on trade ties. As a selected example, on the 20th March 2014 the EU had 52 anti-dumping measures and three anti-subsidy measures in force against Chinese imports. (European Commission, 2014) While many German automakers – such as BMW (Barkin & Rinke 2014) – sell more cars now in China than in Germany, the European Union has a staggering deficit of trade against China of EUR 180 billion (European Commission, 2016).[1] It is attributable to multiple reasons including the nature of global value chains (GVC), but also government-linked economic practices within China in a wide range of sectors. The EU lacks transparency and genuine market access from the Chinese side, and sticks to the rule of law in its bilateral trade dealings, whereas China claims it adherently lives up to its WTO-obligations, and claims its Market Economy Status (MES) in its commercial dealings with the EU.

The EU has well-established resolution mechanism under the WTO principles in place to handle a wide scope of trade issues on behalf of its 28 Member States whether internal or external. The EU's common trade policy has been widely regarded as the single most important, and successful field of cooperation of the bloc. However, with the 2008 global financial, and ensuing economic crises the European integration process was shaken, and internal divisions of the bloc have become more apparent and conflicting. With the Brexit, the parallel emergence of China's economic might, and Chinese home-grown products increasingly turning competitive rather than complementary in their nature to their European ones, the EU has come to a crucial point in

1 According to the National Bureau of Statistics of China the EU's deficit with China did not reach 140 billion euro in 2015. (China Statistical Yearbook of 2016.)

determining not only its China policy, but the bloc's common economic fate en masse. China's rise as a challenge to the fragmented EU is yet to be addressed.

The EU is at a critical juncture of its development, where its relations to China are of special relevance. Neo-liberal and neo-realistic approaches of international relations provide with differing answers on whether the two are headed towards a necessary economic (and political) conflict. However, in a rough theoretic interpretation, the UK can be seen as opting for a more neo-liberal approach to China, whereas a larger chunk of the European mainland – championed by Germany – tends to turn to a systemic way of economic protectionism. This is but only one of the major ruptures within the bloc that is exemplified by the members respective relations to China. The current paper does not seek to analyse the EU's economic issues with China in its complexity, nor can it present a thorough historic interpretation of bilateral trade relations. It can, however, point out certain historically resembling patterns, that may be understudied or even unrealized by history- or current trade-focused researches. The current paper draws more attention to six historical parallels, that are seen to be related to current developments, and which could potentially prove to be beneficial in addressing the necessity of a common European response to China's economic rise. Besides introducing the historical parallel itself, each of the six parallels has strong focus on the present by underlining current opportunities and threats. The paper concludes with policy recommendations derived from the six parallels.

3. Aspects – Reflections of History?

3.1. Trade Deficit

The Chinese market for coins, essentially, set the global standard. Ken Pomeranz and Bin Wong from the Colombia University argue (Pomeranz & Wong, 2004), that while mines in Mexico and Peru were the source of up to 85 percent of the total global silver production between 1500 and 1800, much of that silver – 33 to 40 percent of the world's total – eventually wound up in China. The main reason for that was China's enormous trade (in goods) surplus with Europe. The British in the 18th century found a comparative balance by selling woollens and Indian cottons to China, however, tea soon became the single largest commercial item resulting in a shortage of silver. Britain, the globe's number one sea power of the time, had no other way but to go into war with China to force their – inter alia – opium on the empire.[2]

2 http://www.bl.uk/reshelp/findhelpregion/asia/china/guidesources/chinatrade/

China's trade surplus of the past decades show a quite similar pattern to that of those centuries, which is embodied in the country's gigantic forex reserves topping at close to USD 4000 billion in 2014 (State Administration of Foreign Exchange). Pomeranz and Wong come up here with another key thought:

[The Europeans] started looking for something else to export to China and found that they were in a real bind because there were very few things that they produce more efficiently than the Chinese could.

That is perhaps the largest hidden fear of the Western economies in regards to China's economic –(re)rise in the 21st century. Once the Chinese economy entirely evens out in terms of technological advancement with that of the developed world, the Chinese will have the upper hand in all major sectors of modern economy simply because of the logic of economies of scale. In electronics and manufacturing this is already a tangible phenomenon. As Hans Kundnani, a fellow at the German Marshall Fund in Berlin puts it "They've [Germany and China] increasingly become competitors in similar, high-end production areas". (Delfs, 2016)

In the comparatively new renewable sector, China caught up with the technological level extraordinarily quickly, boasting today of the largest solar and wind plant manufacturing plants. Although the sector's national regulations combined with differing feed-in policies may potentially distort the markets, IHS and the Joint Research Centre (JRC) already have pointed out that

European producers cannot keep up with their Asian (not just Chinese) competitors, because of their lack of economies of scale. European producers have to consolidate themselves into bigger outfits or concentrate on niche markets and/or added value. (Lorenz, 2016)

Some other, more traditional sectors also face a flood of cheap Chinese produce. Perhaps the two most spectacular and debated ones are the aluminium and steel manufacturing industries. In both cases China sustains immense overcapacities, and is reluctant to curtail them significantly. European aluminium producers claim that Chinese overcapacity in primary aluminium is five times the size of the EU's entire production (Michalopoulos, 2016), whilst the same figure for steel is calculated to be at around 400 million tonnes (EUROFER 2016), comparing to a total EU annual demand of 155 million tonnes. The problem with China's surplus here is that it largely derives from systematic state subsidies, while operating with a relatively and absolutely larger environmental footprint. The steel industry issue is further discussed at the 3rd parallel.

While threats to traditional and newer European economic sectors seem to be apparent, there are many factors and trends that alter the overall picture.

- One of them is, that Chinese forex reserves started to sharply decline in the past years (State Administration of Foreign Exchange). Although this is largely attributable monetary interventions on the financial markets in times of large fluctuations in the RMB-rate, and Chinese stock exchange turbulences, China is also ratcheting up its FDI outflows worldwide. It cannot be claimed any more that the Chinese only pile up the "silver" and keep the rest of the world from it.

- According to the European Commission (2014) about half of China's exports are produced by foreign invested companies. Although European investments in China tend to serve the domestic market, other Asian and American companies are more actively engaged in China via their GVCs.

- European exports to China are also on a steep upward course, which support millions of European jobs. Chinese consumer retail market has grown to RMB 23,660 billion (USD 3429 billion) in 2016 according to the National Bureau of Statistics of China. (2016.)

- China is not just selling, but also buying. China is a major buyer of European cars, wines, luxurious products. Although Asian tiger economies are deeply integrated in China via their companies' GVCs, their products are also way more customized to Chinese consumers, which enables them to outscore their European competitors on certain Chinese market segments.

It seems apparent that there is room for more European products in China's growing consumer market, for which more efforts should be made. However, the situation is more complex than that. The second aspect draws attention to another historical parallel.

3.2. (Modern) Tributary System

The second historical aspect is the Sino-centred tributary system and the fear of its modern era revival. The cultural and economic unifying force of the East Asian space had been imperial China for approximately two millennia. Imperial China had been the centre of a wide tributary system that (periodically) encompassed an area stretching from the Strait of Malacca, through Himalayan states, to Japan. (Andornino, 2006) The system – dating back to the Han dynasty over 2000 years ago – was built on the basis of trade links, but it had worked as the transmitting network of culture, too. (Zhang, 2013) The system was essentially based on the recognition of Chinese superiority in the inter-state links, whoever wanted to thrive economically in the region, had to have strong trade links with the Chinese empire, hence had to formally subordinate itself to it. Trade relations with China was traditionally more important to foreign nations, and powers than to China herself. This is well represented by the so called Canton System (Van Dyke, 2007) under Chinese authority, that governed and defined Western trade with China for much of the pre-Opium War Qing-era.

Articulated or not, the main Western concerns regarding China's emergence as the world's number one trader are whether eventually China is going to again dictate the rules of Asian, as well as global trade or not. There are certain signs that point to a modern-day revival of the Sino-centric tributary system, yet, it remains undecided whether these converge into a pattern, and if so, how that would affect global trade at its bases: the rules. As already pointed out in the first aspect, Asian economies seem to perform better when it comes to capitalizing on trade with China compared to their Western counterparts. The signs that it take the shape of the once tributary system include:

- Japan and South Korea. Japan has over triple the size of the South Korean economy, yet, the latter tends to outperform the island nation in trade (in both volume and surplus) with China in the previous years, which is largely attributable to the fact that South Korea did not have any serious political friction with Beijing. Japan did. After the 2012 diplomatic crises with Japan over the Senkaku/Diaoyu islands – touching upon the issue of China's territorial integrity – bilateral trade ties entered into a rather stagnating phase, and Japanese FDI has been largely diverted from China towards South and Southeast Asia (World Investment Reports, 2014, 2015, 2016). Talks on a Sino-Japanese-Korean trilateral free trade agreement (FTA) came to halt in 2012, and are yet to regain impetus (Liu, 2016). In the meantime, China and Korea concluded their FTA, skyrocketing already strong trade links, and firing the Korean economy at its highest speed. However, with the decision of the deployment of the American THAAD system on South Korean soil (Lee, 2016), companies start to raise fears over potential trade backlashes from the Chinese side. One of Korea's largest corporations[3] has been already warned by Beijing (Blanchard, 2017).

3 Lotte is supposed to hand over vast areas of its golf courses for the THAAD deployment.

- Taiwan. The island of Taiwan was one of the largest relative beneficiaries in trading with China under Ma Ying-jeou's Beijing-friendly governments (2008-2016). The two sides of the Taiwan-Strait concluded over 20 bilateral economic agreements including the Economic Cooperation Framework Agreement (Albert 2016), and 40 percent of the islands exports (Taiwan Ministry of Economic Affairs) were headed to China. Yet, since Tsai Ying-wen's government has been shown to be reluctant to play by the political rules set by Beijing – i.e. to explicitly recognize the One China principle –, trade volume between the two started to decline, and is set to fall further. This, and the overall fear of economic overdependency on China – similarly to Japan – prompted the Tsai-government to implement its New Southbound Policy to encourage Taiwanese investments in Southeast and South Asia.

- The ASEAN. China has also concluded its FTA with the ASEAN, resulting in a large-scale boom in bilateral trade. Despite the fact, that many of the bloc members have territorial disputes with Beijing over different swathes of the South China Sea, only Vietnam and formerly the Philippines were vocal in opposing China's excessive claims, and none of them dared to militarily question Beijing's growing physical presence. Whereas Japan still controls the waters of the Senkaku/Diaoyu islands on the East China Sea, neither the Philippines nor Vietnam was able to challenge Chinese push in the Scarborough Shoal (Mogato 2015) or the Paracel Islands (Lee, 2016) respectively.

China is increasingly taking a more pro-active role in shaping new trade and investment blocs including the Regional Comprehensive Economic Partnership (RCEP), where rule-based trade will be a crucial point in question. The examples raised are limited to the incomplete description of China's immediate neighbourhood, and it can be argued, that China can flex its economic muscles only when dealing with its comparatively smaller adjacent economies that are closely tied to it. Big players such as the United States, and the EU have the potential and due leverage to stand up against political-linked trade rule setting practices of Beijing, yet, China is becoming more assertive towards Western countries and companies as well. This brings us to the third historical parallel.

3.3. Closing the Gates towards West

China has always been historically cautious about the West (and North), which is best represented by its millennia years old Great Wall project. However, the wall served its due protection against aggressive tribes mostly from the Central Asia heartland.

When China met with more Western traders, it simply assumed they were just some other states from the outside barbarian world wanting benefit from trading with the heavenly empire. Western powers reluctant to fit into its tributary system – described in the second aspect – were simply refused. Emperor Qianlong, of Manchu origin himself, famously replied to King George III of England in 1792 to the latter's request for a British diplomatic representation in Beijing, the easing of trade regulations, and the opening of more Chinese ports to trade: "Our Celestial Empire possesses all things in prolific abundance and lacks no product within its borders. There is therefore no need to import the manufactures of outside barbarians in exchange for our own produce."—Qianlong Emperor (Modern History Sourcebook)

Up until the Opium Wars European traders had to accept not only their formal subordination to the Chinese Emperor, but also abide by the ever-changing rules and regulation of the Chinese administration system. This, in itself, wouldn't make much difference to just any other nation that wanted to trade with China. Despite some relatively minor atrocities and marginal clashes with the Portuguese, it wasn't until Western powers managed to force China to accept their rules for trade, that the tangible problems regarding the West emerged in the Chinese imperial court. The rise of anti-West sentiment within China and its court was inevitable, and resulted in a number of movements against those powers, most notably the Boxer Rebellion (1899-1901).

President Xi Jinping's anti-Western stance is becoming embodied in numerous fields inside China, including calling on universities to refrain from textbook of Western values (艾 – Ai, 2015), limitations on foreign film industry produce (Beech 2017), or lately the denouncement of the idea of an independent judiciary and the warning of judges not to fall into the "trap" of "Western" ideology by Chief Justice Zhou Qiang (Chinanews, 2017), tightening the control (Ye, 2017) on Western online sites, and services. These were always the things foreign endeavours needed to live with in China, but what feels more worrisome is the tightening control on business activities, such as Beijing's new cybersecurity law.[4] While Western countries and their corporations call for the improvement of Chinese market access and transparency, it is perceivably changing for the worse. A growing number of Western companies feel that they're not so much welcome anymore in China.

The South China Morning Post ran a couple of articles on how and why Western (and Japanese) companies tend to seize or cut back on their Chinese operations,

4 https://www.bloomberg.com/news/articles/2016-11-07/china-passes-cybersecurity-law-despite-strong-foreign-opposition

much because of the worsening political environment. Remarkable examples are McDonald's selling its operations to a Chinese company (People's Daily 2017), L'Oréal, Germany's Metro, or Japan's Sony closing shops (Li, 2017). Long-time European champions on the Chinese markets, German companies are also losing confidence in their Chinese expansion and presence. Germany trades more with China than France, the UK, and Italy do combined, yet, as the director of the new Mercator Institute on Chinese Studies in Berlin, Sebastian Heilmann puts it, the honeymoon period between Germany and China is at an end, e.g. because of intensifying consumer protection crackdowns.

There is a degree of disenchantment setting in. Many managers are being forced to recalibrate: instead of racking up record sales, they are suddenly being forced to cope with structural change and cost cutting. (Barkin & Rinke, 2014.)

Those are not only the Germans from Europe to experience a business climate change in China. According to a 2015 survey of the European Chamber of Commerce in China "only 47 percent of European businesses plan to expand their China operations (...), down from 56 percent last year [2014] and 86 percent in 2013." (Stanzel, 2016, The European Union Chamber of Commerce in China, 2016) The president of the Chamber, Jörg Wuttke said in 2016, that "We have never experienced so much pessimism." Another poll reveals that about 70 percent of E.U. companies "feel less welcome in China than 10 years ago." (Scheuer & Riecke, 2016)

Why is that? Why is anti-European (business and political) sentiment growing in China now? The outlined historical parallel drawn up might be apt to understand the trends. Just as some centuries back, there's a fundamental difference between Western powers' and China's motives in their bilateral relations. Whereas European historic interests to and in China were, however predatory, basically business-driven, the Chinese remained power-centred at their core, and thus political in nature. If we take a glance at the current "core interests" of the EU and the PRC, we find a very similar, but more tinted pattern today.

Europeans, and Westerners in general have quite an accentuated set of principles of what they regard as a market economy, and clear-cut rules of how they wish/want to engage in business, may it be trade or investments. The EU's key concerns regarding China is briefly summed up by the European Commission's country profile on China (European Commission):

- lack of transparency;
- industrial policies and non-tariff measures in China which may discriminate against foreign companies;
- a strong degree of government intervention in the economy, resulting in a dominant position of state-owned enterprises, and unequal access to subsidies and cheap financing;
- inadequate protection and enforcement of intellectual property rights in China.

Although China formally recognizes the principles of a market economy as achievable goals, and it did liberalize its economy massively compared to its Maoist state in the 1970s. However, most of the former East European communist bloc managed to turn their economies to being essentially market-driven within less time, where China clearly falls short of abiding by many of those requirements. According to the World Bank, the Chinese government continues to exercise control over prices for transport, energy, utilities, credit, and land in particular (Yoders-Reisman-Heinzmann-Berezowsky, 2016). A 2016 Wall Street Journal analysis of nearly 3.000 domestic-listed Chinese companies claims, that "reported government aid rose to more than 119 billion yuan, or more than $18 billion, last year [2015] compared with about 92 billion yuan in 2014." (Spegele & Miller, 2016)

Beijing holds back economic reforms politically. At the same time, however, China is not indifferent anymore towards trade relations with Europe – as it historically used to be. It is deeply interested in the maintenance – and increase – of good trade ties with the European Union, its largest trade partner. It also hails win-win type engagement with the EU in its strategic Policy Paper on the EU (MOFA 2014), and expects it to recognize China's market economy status (MES) in accordance with the due "expiry of the surrogate country approach" 15 years after its WTO-accession. (Global Times, 2016.) The question arises of why then China doesn't act in line with its key economic interest, i.e. fulfilling the criteria for the market economy status? Why does it appear so belligerent towards Brussels regarding the issue of the MES? It is difficult to be provided a simple answer to this question, but it is closely linked to where it fundamentally differs in its attitude to the EU: politics. While the EU has clear core interests specified in trade and investments, China does have its officially stated core interests in the arena of politics.[5] These are state sovereignty, national security,

5 One of the symptoms of China's supposedly politics-dominated approach to trade issues is its characteristic attitude when it comes to trade disputes, which is widely seen as 'tit-for-tat' in the West. Some examples: In 2008 the European Union banned Chinese soy-bean imports over high levels of toxic substances, a week later Beijing declared a shipment of Belgian chocolate "not suitable for human consumption" along with blockage of Dutch soybean powder, Spanish dairy products, Irish pork

territorial integrity, national reunification, China's political system established by the Constitution and overall social stability, and basic safeguards for ensuring sustainable economic and social development. (State Council Information Office of China 2011.)

China clearly links social stability to certain practices of state role in its economy – e.g. the employment facet of its state-subsidized steel industry was brought up by president Xi Jinping at his joint press conference with James Cameron in London, 2015, even the question was addressed to Cameron (CGTN 2015). China also feels badly contained in several of its core political interests – including the South and East China seas, and Taiwan – by the USA. Washington also happens to be still the ultimate guarantor of the EU's security in the background, which keeps the EU in a definable room in its foreign policy dealings. Being as economically fragmented, politically weak as it is, Brexit-shaken EU has failed to live up to a role Beijing (would have) wanted to see it taking: a counterbalance to Washington's might on a global stage. This is certainly at least one of the largest reasons behind growing anti-European sentiment within China. As the Chinese economy evolves into something closer to Qianlong's above vision, Beijing seems to tap on the dividing lines within the European Union more and more assertively.

3.4. Fragmented Europe

The fourth historical parallel lies in how well China reflected the divisions of European nations at the height of the global colonial era, in a similar way as it mirrors Europe's fragmentation today. European commercial presence was very strong in the late 19th century China, and it is vital in the early 21st century. China was big enough to 'accommodate' the different Western powers without them engaging in serious fights with each other over China. European nations were only willing and able to unite, and commonly act in China when they needed to protect their unequal treaties against the alliance of the Qing Court and the Boxer rebels. Other than that, European presence in China is best described as rivalry, and only reflected the intra-European frictions, that eventually reached their destructive plateau with the two World Wars.

and Italian alcohol; (http://www.expatica.com/be/news/Belgian-chocolate-banned-from-China_157255.html) In 2011 the EU imposed duties on Chinese steel-tubes, which was followed by a similar step from the Chinese authorities against EU-produced steel-tubes within just weeks (McDonald-Gibson 2013); China launched a trade investigation on imported European wines within a day the EU announced its preliminary import tariffs on Chinese-made solar panels. (Bradsher, 2013)

Although we cannot find the same spheres of influence today, a similar pattern can be observed when European nations engage in commercial links with China. As mentioned earlier, Germany was the pioneer among European countries having advanced with its business interests in China since the start of its opening up policy. Germany today conducts "government consultations" with Beijing involving a wider scope of the political elites than the similar annual dialogue between Beijing and Washington. This mechanism has been unique among European countries, including the European Commission. (Hille & Wiesmann, 2012) Merkel visits China on an annual basis, and is usually accompanied by the largest German-based TNCs such as Daimler, or Siemens. These visits provide opportunities and venues to sign several intergovernmental agreements as well as business deals totalling normally well above EUR 1 billion, like the latest in 2016 of EUR 27 billion. (Stanzel, 2016)

The French march close to the German footpath. France was vocal supporter of the EU's closer ties with China, and came first among Western nations to establish "comprehensive strategic partnership" with China in 2004. (Ju, 2014). No wonder. As an example of the beneficiary relations, Wu Jiao, and Li Xiaokun of the China Daily reports (2010): "In 2007 … Hu, together with his French counterpart, Nicolas Sarkozy, officiated at the signing ceremony for deals totalling 16 billion euros ($22.8 billion) on Thursday at the Elysee Palace. The contracts included … 1.18 billion euros of telecom equipment and the sale of 20,000 tons of uranium from France's Areva to China's Guangdong Nuclear Power Corp."

The UK is regarded as rather a latecomer to establish closer links with China; however, it is stepping up the pace to catch up with its European rivals. It was as late as 2010 when the first large-scale business delegation of over 40 executives from Britain's biggest companies set out for China with PM David Cameron. (Foster & Moore, 2010) They returned home with not much more success than envoy Lord George Macartney some 200 years earlier (Hevia, 1995), yet, in 2015, when president Xi Jinping made an extremely high-profile state visit to the UK, about £40bn worth of deals have been pocketed. Many of them controversial though. (Inman, 2015)

China was not to blame for the divisions among European powers in the past, nor can it be the scapegoat today. So why is this problematic then? Why isn't it just normal for European nations to deal with China independently? In a world where business links would be entirely based on fair trade and proportionately mutual benefits, and where political interests and values wouldn't come into conflict, probably it would. However, as Alibaba Group executive chairman, Jack Ma, pointed out at the World Economic Forum in Davos, "the United States has gained tremendously from globalisation, but has squandered the benefits by not spreading the rewards throughout society". (Zhou 2017) More importantly Chinese president Xi Jinping also outlined the flaws of globalization in his widely-watched speech in Davos (Xi 2017), implying that the Washington-dominated international systems failed to deliver in terms of just global development. Beijing apparently doesn't want, and won't let globalization be unjust to China, which is just natural, and right. However, as long as it does not see a reliable partner in the EU to counterbalance Washington's might – which it sees as the largest threat to its core interests introduced in the third historical parallel –, and to shape a more just international system, it is more likely to sustain unfair trade practices, and make use of the divisions within the EU. Given the fact that power balance between China and its European peers has greatly shifted to the former's favour compared to the late 19th century, the EU can be seen as highly vulnerable as a political-economic entity in this relation.

This points to the much more complex and structural internal problems of the European economic and political integration, which, again, the current paper cannot address. It can, however, briefly point out the ways China would potentially exert its increased influence – both political and economic – on the divided EU. Economic and political ties between the EU and China are broad and very complex, which means, that in the case of a possible trade war, the EU would also have a lot of leverage on China. However, the EU's vulnerability lies also largely in the complexity of the ties. With its autocratic regime, central policy planning, and distribution system, Beijing can more easily cushion the shocks of a possible single sector trade war with the EU, whereas it takes usually nine months for the European Commission to impose defence instruments (Valero, 2016).

There are six major ruptures within the EU, where China already shows signs to make use of:

- Old vs New member states. Many of the countries that joined the EU after 2004 seem to be trapped in the middle-income-trap, failing to truly upscale their economies and integrate deeper into the more advanced parts of the bloc. China's move to establish its 16+1 framework is seen in the Western side of the EU as a move to address and make use of that division.

- North vs South. Most of the EU's (old) Southern members also showed signs of lagging behind, which was amplified by the 2008 financial crisis, fears of the domino effects of a possible Grexit, and the ensuing European sovereign debt crisis. China was quick to engage in those countries, buy euro bonds, and make such strategic infrastructural investments as the port of Piraeus is Greece.

- West vs West. Within the sphere of the EU's comparatively well-doing members, two major blocks have been formulated: one with the lead of the UK calling for a more liberalized trade regime, and the other being championed by Germany and France hailing a more protectionist approach. Although the Brexit has mostly been driven by domestic factors of protectionist nature, it shall not be forgotten, that with the leave of the UK from the EU, Brussels is losing its most vocal and powerful advocate of international free trade. China's role, and stance is elaborated in the fifth historical parallel.

- Intra-country, and inter-sectors division. A remarkable example on that phenomenon is the solar panel dispute. The next day the EU announced its preliminary import tariffs on Chinese-produced solar panels – protecting mostly German manufacturers –, China vowed to launch an investigation on wines originating from the EU (Bradsher, 2013). Beijing's move naturally unsettled European – for all French – winemakers, but it also rang the alarm bell among German carmakers, and other German firms with a big presence in China as well. Both groups – the wine and the car industry – started to lobby, the former in Brussels (Bradsher, 2013), the latter in Berlin to "prevent a full-blown confrontation" (Barkin & Rinke, 2014).

- Values. Although the European Union's 2016 strategic papers on its relations to China (European Commission 2016; European Council 2016) outline the bloc's dedication to value-based economic, political, and social engagement with China. It finds it increasingly difficult to hold onto its own principles, which shows a more worrisome dimension of the EU's disintegration. According to a leaked American cable, the lifting of arms embargo – imposed by the EU on Beijing after the 1989 Tian'anmen square crackdown – was supported by numerous member states as early as 2004 (Rettman, 2011). Another spectacular issue is the case of the Dalai Lama, who is a recognized spiritual leader in the West, and seen as a belligerent separatist in China. After meeting the Dalai Lama, European leaders including Angela Merkel (2007; Barkin & Rinke 2014), Nicolas Sarkozy (2008; Day 2008), or David Cameron (2012; Odell 2015) all had turned less vocal on human rights issues, and made significant efforts to comfort the Chinese leadership that normally puts bilateral ties into deep-freeze following such meetings.

- Security. The EU's inability to show a united approach on Beijing's core interests – introduced in the third parallel – leaves the block helpless to act as a peace-agent between the United States and China, should the two militarily confront each other. In 2015 Beijing and Washington managed to successfully divide the EU on the participation in founding of the Asian Infrastructure Investment Bank (AIIB) – seen as a major pillar of China's external economic strategy –, or when the EU failed in 2016 to unequivocally denounce Chinese claims on the South China Sea (Emmott, 2016).

This is not to say that the EU is necessarily heading to fall-off, or an utter trade or other confrontation with China. However, the lack of central coordination of its members' China-policies, and China's mere size leaves it vulnerable in multiple regards, and history warns the old continent. The fact that European nations were only able to form a united front in China when they came under attack – the Boxer rebellion in 1900 –, does not augur well for today's divided EU. That historical unification of forces resulted in extensive looting of Chinese imperial treasures, as well as in the continuation of unequal treaties with Beijing. After WWI, and more so after WWII, European powers failed to uphold their influence in China, which leads to the fifth historical parallel.

3. 5. Europe: Cutting the Branch It Is Sitting on?

The fifth (and sixth) historical parallel follows from the fourth. Europe's strong presence in China faded after its nations fought their first World War. That is, European countries failed to resolve their differences, and as a result, they weakened each other. Europe seems to be self-shooting itself today again with the Brexit as it falls short of recovering from its structural divisions, and its economic leverage it still sustains over China may, again, fade.

While Britain might enjoy some benefits of its exit from the EU, its position as an economic and political entity will certainly weaken. Ivan Lidarev expects (1) the UK to weaken its significance as an influencer of EU-politics – an asset worth much for China – fades. With Brexit Chinese companies (2) potentially loose springboard to the highly regulated EU markets. London (3) may also lose some from its strategic importance as a European centre for the internationalization of the RMB. (Lindarev, 2016.)

On the other hand, the EU finds itself weaker without the UK, too. The Japan Times quotes David Warren, a former British ambassador to Japan and chairman of the Japan Society in Britain as saying: "I think the European Union will miss Britain's presence in negotiations with Japan and China. It is a major world economy and a force for global liberalization. … And I believe Brexit weakens the EU-U.S. alliance (against China) because an EU without the U.K. is inevitably a weaker political agent in the world. A weaker EU is in no one's interest." (Hollingworth, 2016)

Nor is a weak EU in Beijing's interest. The Chinese stance on Brexit has been widely discussed in media and academic circles. Although Beijing can clearly benefit economically from a divided EU, it certainly has a strong stake in upholding the bloc's functionality and pure existence. Hungarian former ambassador to China, Sándor Kusai said in an interview (Buzna, 2017): "Beijing has an interest in an EU being able to make independent decisions on global issues, which apparently assumes some form of unison. At the same time, it is also interested in that the EU wouldn't confront Chinese interests. In accordance with that China naturally wants to influence the processes of the EU."

Beijing's attitude may seem ambivalent, yet, it is very aware of how much impact the EU's stability has on its own stability – the core of its core interests. This goal of China is also presented in its current strategic Policy Paper on the EU adopted in 2014. (MOFA, 2014.)

China and the EU, the world's most representative emerging economy and group of developed countries respectively, are two major forces for world peace as they share important strategic consensus on building a multi-polar world. China stands ready to provide necessary support in various ways to the stability of the European financial market.

This reflects Beijing's wish that the EU would form a counterbalance against Washington in a multipolar world. Brussels failing to live up to such Chinese expectations may lead to Beijing trying to divide the West in large. There are already signs of China playing cards with Boeing and Airbus when it comes to core political issues such as the Dalai Lama. (Liu & Zhou, 2017; Wu, 2017.)

Airbus is the flagship of successful European economic cooperation, as well as a symbol of how much is threatened by the Brexit. Despite all the divisions within the EU, and independent policy-making of their nations, there has been at least one major largely common European project, that has worked sufficiently in the China relation as well: Airbus. The Airbus has been the common denominator of the EU's largest economies, which has also been represented unprecedentedly successfully. Tony Blair[6], Nicolas Sarkozy (Wu, Li 2010), as well as Angela Merkel (Dalje, 2015) all sealed deals for the pan-European company worth billions of euros. Airbus, however, couldn't have possibly become a joint political goal for key European leaders, hadn't it been a viable business venture itself. As Sandy Morris, analyst at Jefferies puts

6 http://news.bbc.co.uk/2/hi/business/4217888.stm

it (Tovey, 2016): "European co-operation projects don't have a terribly good history. Airbus is a fascinating one that's become a success – eventually. That it worked at all is a miracle."

With the Brexit, free flow of goods, spare parts, and the employees of the company is undermined, threatening the viable operation of the UK business. Airbus has about 15.000 employees in the UK (Monaghan, 2017), and supports further 100.000 jobs in the country through its extended supply chain of 400. (Blanchard & Osborn 2013.) Although the company's senior management released a statement (Kaminski & Morrow 2016), in which it pledges to "minimise any impact on [its] operations". Its opening lines are telling: "We respect the decision taken by the British people, which should be seen as a wake-up call for Europe and as a catalyst for change."

While Airbus itself operates a factory in China, the appearance of indigenous Chinese competition (SCMP, 2017) embodies the challenge the European economy – and politics – is about to face in regards of China in all the historic aspects that have been introduced. The five parallels point towards a sixth one, that is yet to entirely unfold. That is the ancient Silk Road, and its present-day revival proposed by Chinese president Xi Jinping. Not that trade volume between the two ends of the ancient route wouldn't already exceed all previous levels, it is rather about a more conscious, planned, and controlled shift of the main axis of the global economy to Eurasia. In that regard, China's major interest is the freest possible flow of goods along the route, while the EU's best interest is a comprehensive Bilateral Investment Treaty (BIT), that would secure a level playing field for Western companies in China. Beijing vows to carry out the vast agenda based on cooperation, and mutual benefits. Europe is yet to grow up to such large-scale thinking to be able to take its proportionate share of control on the process, but that requires more cohesion. The Silk Road was a trade route that was a win-win project of its time, but then Europe – the only time in pre-Treaty of Rome history – was largely united under the Roman Empire.

4. Policy Recommendations

The aspiration for a unified policy position in Europe toward China is a holy grail, or something like alchemist's gold. The issue is who, precisely, would forge this. "... The best they [EU-member countries] can do is to look after their own national interests, while trying to tie those into the EU interests generally — a hard task."

These are the words (McDonnell, 2014) of Kerry Brown, Director of the China Studies Centre at the University of Sydney, suggesting that the drive for a common European policy has been there for long. The question is not only who would forge the differing interests of the member states, but also how to do it. The EU is attaching more importance to the issue than ever before, which is represented in its 2016 strategic document policy paper. Points such as "improving analytical capacity on China" or that "the EU's strategy on China should be reviewed at regular intervals" reveals that the importance of the matter is more consciously recognized, and being addressed.

The need for a common EU policy on China can be interpreted as an opportunity as well as a threat. It is an opportunity, as China's rise to a global economic powerhouse naturally pushes Europe to attach due importance to it, while – as a former senior Hungarian diplomat to Beijing, Gyula Fazekas once told me – China should be far, and big enough to make the members able to align their differing interests. Brussels, on the other hand, should keep in mind that the facts that (1) China is an autocratic country, and (2) it is already the globe's no-1 economy on purchasing price parity (PPP) can potentially make it less accountable.

The purpose of the current paper is not to present the "holy grail", but to draw attention to the EU's well-known vulnerabilities from historical perspectives. Although policy recommendations are formulated based on the findings, those are either to ignite more new thinking on the issues, or to shed light on an already existing policy recommendation from a different angle. The primary goal of the paper is to underline the importance of the lessons lying on the ground, that history has already provided Europe with, and to point out underrated skills of the European integration. The six historical parallels introduced in the paper are divided into two categories that cover internal problems and external challenges for the EU in its relations with China.

4. 1. Internal Problems

The fact that one of Europe's largest powerhouses chose to walk its own way is a clear sign of that the EU – not necessarily the UK, or not just the UK – as an organization is sick. Chinese medicine might help, but it certainly has a high price. The Brexit, however, is only the tip of the iceberg, as the European Union remains deeply divided in several aspects, China, or the 2008 crisis are not to be blamed for the EU's internal problems. Signs of incapability of the EU to resolve its structural problems comes at a time when increased unity would be required to withstand increased competition from the Far East and protectionism in the United States. External challenges certainly amplify the Union's internal matters, reveal its vulnerabilities, yet, they are not the source of them. Hence it is assumed, that (1) internal problems have to be sufficiently addressed in order to successfully cope with rising external challenges.

As the six historical parallels represented, China's rise force the EU to adopt different, broader ways of thinking regarding its external policies, that requires internal unison. It is also assumed, that (2) the EU is at a critical juncture in the late 2010s. Either it will be able to bring its integration project onto a new level, or it has to face disintegration. China faced a similar juncture in the early 1990s, when the leadership, hallmarked by Deng Xiaoping, decided to continue, and deepen the economic reforms. It is commonly believed that Beijing made the right decision. A possible disintegration of the EU today could turn out disastrous not only to its member states, but to the global economy as well, hence no one is interested in the disintegration of the bloc. This brings us to the conclusion that the only way forward is to deepen the bloc's integration process, which should address the EU's key structural problems, and designate Brussels' place at the global economic as well as political stage at the same time. In the following part an outline on how to address the major divisions within the EU will be sketched.

- Old vs New member states: a more efficient agenda shall help the struggling states catch up with the developed ones; at the same time new member states shall secure a seat for Brussels within the framework of their co-operations with China, that is broadening the 16+1 to 16+1+1.

- North vs South, Security: another competitiveness agenda shall support the EU's southern members to carry out a comprehensive economic restructuring; at the same time, it also has to adopt supranational security policies to protect e.g. key infrastructure defined as of strategic importance.

- West vs West: as briefly introduced in the "Divided EU" section, there are remarkable achievements of the major European economies in their respective relations with China. None of them is willing to give up on those results in the sake of something called common, but not tangible, and would defend them if seen threatened. European economic and political rivalry outside of Europe, however, rarely bore fruits. Airbus remains a rare example of viable cross-European business and political co-operation in regards to China. The key for Airbus' success, coordinated contributions, needs to be decoded, and applied in a broader EU-strategy. Once the countries make a joint attempt to channel those skills and assets helped them achieving their respective success in or with China to help other members, a natural mechanism of capacity, skill, and knowledge sharing could potentially evolve.

If well-facilitated, the mechanism could also incite the countries merge their different traditional skills to achieve more or something common. Values such as meritocracy, shared leadership, as well as participation can be cornerstones of an organic, comprehensive, and widely-recognized European China-strategy. The Airbus-approach applied in the bigger EU shall be institutionalized in a way to minimize, and bridge potential negative effects of the Brexit.

- Intra-nation, Inter-sector divisions: the Chinese economy has to be monitored and analysed on a regular basis to forecast the key competitiveness challenges for the EU's economy. China's anti-trade, investment, and market access measures shall also be systematically documented and analysed, especially those regarded as tit-for-tat moves against the EU or one of its member states. Patterns of Chinese proceedings shall be closely tracked in order to be able to tackle and counter unfair behaviour. This is a highly complex task, but not enough itself. Creating complex defence mechanisms will not necessarily cure the very heart of the problem, i.e. the divisions, which make those measures extremely difficult to implement. Instead the focus should be more on bridging the internal divisions by further boosting synergic intra-EU integration along common competitiveness goals. Representatives of major European industries shall be more directly involved in shaping the EU's global competitiveness agenda to China.

The bridging of the divisions cannot happen overnight, hence ways and mechanisms shall be found, and worked out to prevent third parties – not only China – from strategically benefiting from the divisions. For that matter, the bridging of the divisions shall be approved as the EU's core, region-specific economic strategies with a vision of raising the bloc's global competitiveness through stronger internal integrity. It shall be considered; whether certain practices of central economic planning from developmental states such as Japan, South Korea, and even China can be fitted for, and implemented within European conditions. As the EU's strategic policy paper on China underlines, "active use should be made of the available EU co-ordination mechanisms in order to promote EU unity", this attitude shall apply to the existing strategic papers, including the Europe 2020.

4.2. External Challenges

The external challenges posed by China's rise are introduced in the first three historical parallels, as well as the brief section on the (New) Silk Road. The EU's strategic paper on China addresses the key concerns of the bloc, and the annual EU-China summits, while high-level dialogues secure a platform with China to "set the objectives and priorities to implement the common strategic agenda". In this concluding part, some more political recommendations are offered in line with the historical parallels.

- Once its internal divisions are systematically and successfully addressed, the EU needs to practice articulating and representing its common goals and interests to China with due weight. This is a super power skill the EU has yet to learn – quickly;

- Should there be issues of common concern with third nations regarding China's trade behaviour – as introduced in the first three historical parallels –, where EU and WTO rulings prove to be insufficient to curb unfair practices going against the Union's – and third countries' – core interests, the EU should establish coordination mechanisms with those countries to exert due pressure on Beijing;

- The EU needs to be remarkably more proactive, initiative, and active in large-scale projects of strategic importance, including the AIIB and the OBOR. With the U.S. withdrawal from the TPP, the EU's role as a guarantor of international laws, standards, and democratic decision-making rose significantly. With an active, initiative engagement, it would secure its say in future standards of Eurasian trade, and make sure the goals of the United Nation's 2030 Agenda are being met;

- The EU needs to grow up to think as strategically as Beijing does in the Eurasian economic space, where the major axis of the world economy is clearly shifting to. The EU not only needs to have a common China policy, but in line with that, it also needs to have a common Eurasia policy as well.

- Brussels needs to be prepared for the possibility that major players of the global economy might forge ahead with a partial or complete redraw of existing international rules and practices of trade, most notably the Donald Trump-lead United States. Brussels should stand firm to protect, and to improve commonly approved values and standards such as the rule of law, or the WTO dispute-settling mechanisms.

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Institutional Challenges to the Central Bank of China – a Central European Perspective

Péter Bihari

The Chinese central bank uses more and more market instruments instead of applying administrative instructions. However, due to the difficulty of the transmission mechanism, their effectiveness is limited, and therefore some elements of the manual control are still in use. This paper presents the ongoing easing process of two institutional obstacles of the transmission.

It has been an important experience of central banks of major market economies that what has the greatest impact on market processes is not current interest rate decisions, but rather expectations of future central bank interest rate moves. The degree of central bank independence (CBI) and the openness of its communication have fundamental implications for the evolution of expectations. Without the independence of central banks, market instruments cannot fulfill their function, and a conservative approach to communication weakens the effectiveness of these instruments.

1. The Rationale behind CBI

Traditionally there have been three main arguments supporting CBI:

1. Price stability is a precondition to the realization of the long-term growth potential. Inflation above the price stability level makes it difficult to reach growth potential and has a negative impact on the potential growth rate. The high inflation increases the costs of production and the costs of holding money, distorts income distribution, and makes the future more unpredictable. Inflation below the price stability level also tends to open a gap between actual and potential growth as it has a negative impact on aggregate demand; and increases the real value of debts of economic agents.

   Price stability is not in good hands if the government is responsible for it. Government politicians are more prone to boosting aggregate demand and therefore create surprise inflation in order to strengthen public support for their re-election; to reduce budget deficits. Expansionary economic policies driven by short term political interests may result in higher economic growth, higher welfare of society and higher inflation. However, economic agents adjust quickly to changes in the environment, and in order to protect their real income, workers tend to claim higher nominal wages. If they succeed, a cost inflation pressure will emerge, too. As a result of this, demand and growth in real term will increase only temporarily while higher inflation might persist if expectations change accordingly. Government politicians act against their self-interest (their re-election) if they consider price stability as a high priority target, and if they take anti-inflationary measures with short term negative growth effects. For this reason, it is justified to make price stability the responsibility and overriding goal of an institution independent from government structures. Even in such a case, governments are able to create surprise inflation. Yet the realization of price stability is far more likely if it is being looked after by an institution which is not subject to short-term political interests and cannot be forced to implement instructions motivated by such interests.

Currently, the main problem central banks are facing is not excess inflation, but price increases below the price stability level. Low inflation is partly a consequence of insufficient global demand and is, in part, a result of anchored expectations. Success in controlling inflation expectations is a result of many years of efforts by the central bank. In the absence of independence, expectations are likely to lead to higher inflation. This is because the public knows (or should realize rapidly) that if inflation does not have a good owner, the evolution of prices will move away from the announced goals, therefore people have no reason to anchor their expectations to these goals. That is to say that de-anchoring of expectations can quickly occur, and re-anchoring them again may take a long period of time. Therefore, concerns about the effects of political interference in monetary policy remains valid when inflation is too low as well as when it is too high.

2. Governments, not least as a result of their short-term political interests mentioned above, tend to spend more than their revenues. If governments have an easy access to funding, and especially if this funding is cheap, they will spend boldly and heavily. A narrower and a more strictly regulated access to financing sources is a way to taming expenditures. If the central bank is allowed to lend to the government (or purchase State securities), extravagant spending can continue without any meaningful limits in place due to the fact that the central bank can offer unlimited credit in domestic currency. If the central bank operates in subordination to the government, only the self-restraint of the government can put limits on credit taking. And we know

that vested political interests weaken this voluntary restraint. If, however, the central bank operates outside the government's structures, and it is not commendable to give credit to the government, a more disciplined fiscal policy can be expected.

A significant fiscal deficit can emerge without fiscal financing as well. However, it occurs more easily with fiscal financing in place. This reasoning reinforces CBI from the perspective of budget sustainability rather than that of the effectiveness of monetary policy. In fact, it contains a paradox. Independence means more freedom, while the prohibition of fiscal funding takes away the freedom of using central banks' tools to fund the State. The institutional separateness of central banks can be derived from the monetary financing prohibition. Having recognized his addiction, the enlightened alcoholic stops bringing home alcohol in order to make it more difficult for himself to drink again in his weak moments. (This, of course, does not prevent him from buying the desired substances from the nearby store.) Fiscal alcoholics should also distance the desired financial sources from themselves.

Following the global crisis, there have been large-scale central bank purchases of government securities in many countries. This meant fiscal financing even if purchases took place on the secondary market. The additional demand generated by the central bank pushed the yields down (that was the intended purpose of the purchase) and thus made it cheaper to finance the state, making extravagance less burdensome for governments. Central banks did not act under government pressure. The purchases of government securities were decided in order to promote their own monetary policy goals. The significant negative output and inflation gap temporarily overruled the ban on purchase of government securities. The immediate negative outcomes of the crisis were more severe than the ones deriving from fiscal financing. A practical-minded approach rightly gave priority to fixing the bigger and the more threatening problem. Once the emergency situation was over, the central bank started a gradual ending of quantitative easing. With the restart of economic growth, the reduction of the increased government debt has got into the focus of government policies again. This underscores again the importance of central bank's independence, including the restoration of the ban on fiscal financing.

3. Independence is a necessary condition to the credibility of the primary objective. If central banks can be instructed, the public will be less likely to believe that the objectives will be met. They would believe with reason that the instructions may not always be in conformity with the price stability objective (see above). There is abundant empirical evidence on the negative relationship between the CBI and the inflation.

Monetary policy can contribute to the best exploitation of growth potential by maintaining price stability. Apart from a few short periods, central bank policies have focused on curbing inflation higher than price stability over the past decades. With the intention to put an end to overheatedness due to high inflation, the undesirable redistribution of incomes and unpredictability, monetary policies had acquired, fundamentally, an anti-inflationary character. In the last few years, with weak demand as a result of the global crisis, the increase in consumer prices has tended to lag behind the rate that corresponds to price stability and, in some countries, a negative consumer price index evolved. Too low inflation (and deflation to an even greater extent) increases the threat of a further shrinking demand, a rise in the real burden of government debt (decreasing leeway of fiscal policy), which eventually leads to the conservation of low growth. In such a situation, the best a central bank can do to help preserve growth is to put an end to the negative inflationary gap (a consumer price index deviating downwards from price stability), which could be implemented primarily by creating looser monetary conditions. Too low inflation sheds new light on the central bank's status. Prior to the global financial crisis, central banks were battling against too high inflation. In this endeavor, independence was a useful (necessary) arrangement. Today central banks are battling to bring inflation up to the targeted level. Central bank independence is not an essential element of this effort. It should be noted that the consumer price index is on an accelerating path in China, and according to analysts' expectations, it should exceed 3 percent by 2020.

Obviously, the greater the difference between price stability and actual inflationary processes, the more vigorous rate changes are needed to put an end to it. In the event of strong pessimism related to economic prospects (or a deterioration in expectations), only larger rate cuts can produce the desired impact. In many countries, a higher rate cut would have been necessary than that which was possible since the beginning of the global financial crisis.[1] Radical rate cuts in the United States, Great Britain, the European Union, Sweden and Israel were unable to loosen monetary conditions to the extent that would have been necessary to achieve price stability again.

These central banks then arrived at a crossroads. Should they reach for new instruments bearing the hope of achieving price stability and, with this, violate certain basic principles of monetary policy, or should they take note of the frozen negative inflationary gap and the negative output gap, which would make the central bank violate

1 The leeway of the central bank is restricted by the zero-interest rate threshold, because negative base rates could have the opposite to the desired effect: instead of stimulating it, they rather tend to depress demand. (Bihari, 2013).

its most fundamental mandate. Central banks in the United States, Great Britain and – with some delay – in the Eurozone launched corporate and government bond purchase programs, whereby they pumped extra liquidity into the system, hoping for a decline in government paper yields and simultaneously a rise in inflationary expectations.

The use of unconventional monetary policy instruments and the incorporation of financial stability considerations into central bank objectives both point into the direction of reconsidering the pre-crisis interpretation of CBI. If monetary policy is bound up with financial stability, there needs to be more cooperation and coordination with fiscal authorities.

2. Observed Trends of CBI

Two or three decades ago, almost everywhere in the world central banks operated as a division or under the supervision of the Ministry of Finance. They made proposals which have been transformed into a decision by the ministry's leadership and eventually by the government. Central bank instruments served a multitude of economic policy objectives. They were used to support economic growth and to increase the employment level, to ensure the necessary financing sources for general government expenditures and to manage the balance of payments problems. In many developing countries, the central banks also played the role of a kind of development bank providing long term preferential loans to various sectors of the economy. The price stability and financial stability were also among the objectives, but not as a single or primary objective, but just as part of many other objectives. As a result of the institutional position of central banks, inflation related issues were basically decided within the Ministry of Finance. In highly developed market economies, which followed a conservative fiscal policy, price stability was achieved. In developing economies, where the national currency was pegged to the currency of a low-inflation economy, inflation was low, too. However, in general, loose fiscal policy and inflation in excess of price stability was characteristic of this era.

Within the framework of a planned economy, central banks performed central bank and commercial bank functions simultaneously. They carried out financial supervision, account management and the provision of loans to the corporate sector. The central bank could decide on operational issues at its own discretion, however, longer term or strategic issues fell within the competence of the government, and the most sensitive issues were decided by party bodies. In Hungary, for example, an international bond issuance was possible only with the approval of the Politburo. In Hungary, following the economic reform of 1968, motivated by the intention of separating fiscal and monetary policy management, the National Bank of Hungary got out of the scrutiny of the Ministry of Finance, and from 1968 onwards reported directly to the President of the Government.

As opposed to this state of affairs, in the majority of advanced economies central banks have become almost totally independent by the 2000s. In essence, there is consensus that central banks have a primary mandate to ensure price and financial stability. Without prejudice to this primary mandate, they support the economic policy of the government. They strive to achieve their goals by using the tools available to them free from outside influence. "Although there is a strong case for instrument independence, the same is not true for goal independence, the ability of the central bank to set its own goals for monetary policy" (Mishkin, 2011). The ultimate goal of central banks are (and have to be) decided by political bodies. While using their tools to achieve their goals, they remain free from outside influence. In order to exclude abuse of power and inappropriate operation, the delegation of tasks to unelected bodies of the central bank have been accompanied by increasing accountability and transparency.

It has been a long way from the lack of independence to genuine independence. However, this has not been the road leading to the establishment of a market economy. The misleading relationship presents itself: the more undisturbed the functioning of the market economy, the more likely it is that the central bank's independence will come to fruition. This would mean that in the absence of market framework, there is no CBI; the presence of markets encourages the independence of central banks. The past two or three decades have in fact proved that market arrangements do not automatically lead to CBI. In Great Britain, even in the middle of the nineties, the base rate was determined by the Treasury rather than by the Bank of England. Nevertheless, Great Britain before the mid-nineties was no less a market economy than since that time. Or was it? Cannot the establishment of CBI be interpreted as a further gaining of ground for markets? As the central bank escapes from direct government scrutiny, the autonomy of the economy is increasing, and respectively the influence of political interests on economic processes is reduced. In this respect the establishment of CBI can be interpreted as the further fulfillment of market logic.

CBI has many manifestations, therefore it is affected by many factors. A summarized evaluation should rely on a simultaneous consideration of all related effects. Different texonomies and weighting systems are known. Cukierman (1992) distinguished the following groups of factors (clusters):

- factors related to the status of the governor (appointment, dismissal, term of office, rules of conflict of interest);
- policy formulation factors (who decides on what?);
- factors related to the objectives of the central bank (who sets the objectives?);
- central bank lending factors (limitations on and conditions of the ability of the central bank to lend to the public sector - volume, maturity, interest rates).

Pisha (2011) takes into account the following main areas:

- functional independence (primary and secondary goals);
- institutional independence (decision making process, external influence);
- personal independence (term of office of the governor and MPC members, rules of appointment, dismissal, conflict of interest);
- financial and budgetary independence (prohibition of fiscal financing, budget management and profit/loss allocation rules).

Cukeirman's clusters were built up from 16 variables, while Pisha used 21. Each variable obtained a score and the scores were combined with a weighting scheme in order to determine an overall measure of CBI. The aggregate indicator enables spatial and temporal comparison.

By using the Pisha methodology, Vasile's analysis (2013) of the former Central and Eastern European socialist countries established a high level of CBI lagging just behind the level of independence of ECB. It is noteworthy that by using the Cukierman index Dworsky reached a similar conclusion already in 2000, which indicates that the biggest steps in the creation of CBI had been made in the early stages of transition to a market economy, long before the accession to the European Union took place. Having used and further developed Cukierman's methodology, Dincer and Eichengreen found in 2013 that 8 out of the 10 highest aggregate independence scores were reached by central banks from CEE countries. China was ranked 47th (out of 90 countries). Romelli (2016) developed new dynamic indices of CBI. This new index, called the Extended CBI (ECBI) Index, provides information on 42 criteria of central banks' institutional design. He found that the former socialist economies (East Europe region) were the ones characterized by the highest average degree of CBI in 2014.

However, prudence in interpretation of these results is highly recommended for multiple reasons. Subjectivity in scoring is inherent to these evaluation schemes. Sometimes politicians make hints about desirable central bank interest rates. Should this be treated as a pressure on decision makers? In some evaluation schemes key indicators e.g. "Who formulates monetary policy?" get the same weight as less important indicators. Most importantly, formal end results and real life experience may differ.

3. De Jure vs De Facto Independence

The independence in a legal sense in many cases is not a good indicator of actual independence. The public will sooner or later recognize if a central bank is only independent legally, on paper, but if not based on its real conditions. If monetary conditions are changed as a result of the informal pressure of the government, the independence of the central bank is illusory rather than a reality. Such a central bank may face serious credibility problems and difficulties in shaping expectations. Actual independence is not less necessarily than legal independence. It is also possible that in its practical operation the central bank enjoys greater freedom than one would expect solely based on the written rules.

Numerous real-life examples can illustrate the difference between formal and actual independence. A common feature of these is that the CBI is threatened or strengthened without a clear violation of formal rules.

- Sometimes despite the most independent appointment, dismissal, conflict of interest and decision-making rules the MPC aims at serving government policy goals rather than targeting the price stability. If the Council is composed of members who are servile, do not think autonomously, but give priority to their personal political preferences, or if the governor of the central bank, out of personal conviction or political sympathy, believes that his primary goal is to support government policies instead of price stability, then even without instructions or direct pressure independence is over. In this case, the central bank sacrifices voluntarily its independence without being forced to give it up.

- Even under dismissal rules ensuring the highest level of immunity, early resignation of the governor can be enforced. Open attacks questioning the professional aptitude, the human decency, civic loyalty of the governor may not directly infringe upon the written rules, but it can lead to his or her early resignation. In CEE, the premature interruption of the governor's mandate occured several times. Such precedents may serve as lesson to the next governor and encourage him or her to voluntarily adapt to political requirements.

- Sometimes politicians give their opinion on monetary policy issues. When they comment on interest rates, judge them too high, call for rate cuts or wish to see a particular level of interest rate, intentionally or unintentionally they put pressure on central bank decision makers. Thus, it becomes difficult for them to make unbiased decisions, even if their decisions are strictly grounded in professional criteria.

- The transparency and predictability of the income of the central bank decision makers is an important component of CBI. If the rules determining the income of decision makers are not fixed for the entire duration of their mandate and the actual income may increase or decrease, personal income considerations may become part of decision criteria. Decision makers may want to comply with government expectations in order to get some reward or avoid penalties. In Hungary, the income of central bank decision makers was cut by 75 percent in 2011.

- A legally less independent central bank may be able to enforce its monetary policy considerations effectively if the leader has a great capacity to advocate issues in the central bank's interest as a result of his or her professional preparedness, compelling personal virtue and/or relationship of trust with the prime minister. This independence is primarily based on an informal relationship between the head of the central bank and the head of the government.[2] As this type of independence is linked to individuals, and people change more easily and more frequently then formalized legal rules, this independence has rather limited firmness and stability.

4. The Openness of Communication

Two or three decades ago, the base rate was not always a publicly available information, or if it was, central banks did not consider to necessary to give an explanation to their decision and or an assessment of the economic situation and future prospects. Today, the majority of central banks intensively communicate with the markets and the public through many channels. Various publications describe the strategic framework of monetary policy, its goals, the way how decisions on the base rate are made. The economic considerations behind the decisions are disclosed, central banks' public websites contain detailed statistical data, leaders frequently give press conferences, interviews, and lectures. New findings and recognitions explain this significant transformation

2 Karádi (1999) discusses the independence based on informal bargaining in the context of Hungary.

1. Objectives of the monetary policy can be achieved by influencing the behavior of economic agents. The effectiveness of monetary policy depends on the response of economic actors. The key is not what the central bank does, but rather what the economic agents themselves do. To get the expected response from them it is necessary for the central bank to introduce and explain its current moves and how they fit into the pre-announced strategic framework. Proper communication improves the predictability of the central bank's decisions, reduces their surprise effect and thereby increases the likelihood that the decisions of economic agents get in line with the central bank's intentions. Therefore, communication can improve the effectiveness of monetary policy.

2. Typical monetary policy instruments are bank rate variations, open market operations and changing reserve requirements. During the last two or three decades, central banks recognized that beyond the use of these instruments words were also suitable to make their policy intentions clear and shape expectations. If economic agents can be convinced with words that inflation will be low, then as a result of their actions based on this perception inflation will indeed be low. Therefore, there will be less need to increase the base rate in order to bringing inflation down. Disinflation driven by interest rate hikes has real economic costs such as slower growth of consumption and investment. Disinflation driven by a favorable change in expectations does not have such costs. Communication has become a monetary policy tool helping to shape influence of expectations. If successfully applied, there is less need to use the interest rate instrument. Because of the high social costs of the latter, communication could be an obvious choice for central banks. Communication is more than simply explaining policy decisions. Communication not only supports the effectiveness of interest rate policy, but within certain limits it may substitute it. Communication gains a particular importance when interest rate policy becomes ineffective. Following the global crisis, base rates in many countries hit the zero level, thus this monetary policy tool has exhausted its potential. To further monetary easing, central banks made verbal promises to maintain a low interest rate environment for longer than earlier expected.

3. The intensive communication is inherent in increased CBI. If unelected officials of an independent institution make decisions that have significant influence on social welfare, then their public accountability is a legitimate expectation. Therefore, the broader public must be given detailed information - through annual or inflation reports, parliamentary hearings, press conferences, etc. – on the central bank's objectives, operations, and decisions. Accountability is a tool to exclude abuse of independence and operation against the public interest. Accountability legitimizes

independence, but in return for its independence central banks have to be accountable. In this sense, open communication is an inherent part of the central bank's greater independence. Open communication can be derived from independence; open communication contributes towards the attainment of independence (and makes more difficult to abuse it, too)

4. The consistency, the compliance with the promises, the unity of deeds and words will ensure the central banks' credibility. Communication can strengthen public trust in central banks. A clear outline of how the central bank intends to achieve its goals makes its commitment towards these goals more convincing and more acceptable to the public. Communication and credibility go hand in hand. Communication can only be successful if the central bank has a certain level of credibility. If economic players do not listen to the central bank, communication can only produce empty and useless words. Communication can be both remedy and poison. While good communication builds credibility, poor communication will quickly undermine it.

5. The Communication Practice and the Independence Level of the Chinese Central Bank

In Dincer's and Eichengreen's comprehensive study investigating CBI China ranked 46th out of 90 central banks examined. It is noteworthy that the quantified values of independence for China did not change between 1998 and 2010, while in some other countries CBI increased in the same period. Thus, China has slipped back from the 25th place in 1998 to the 46th in 2010.

Dincer and Eichengreen provided an assessment of transparency for an even larger group of central banks (119 banks). Based on their aggregated transparency index composed of 15 indicators, China turned out to be in the midfield with its 65th place. The change of this ranking is just the opposite of the change experienced in the field of independence. Transparency improved during the decade in question for the great majority of central banks. For China, however, the improvement was significantly greater, that is how after a weak start China could reach the mid-range. At the end of the 90s, in the Eichengreen ranking 99 countries reached a higher score than China.

Transparency studied by Dercin and Eichengreeen is affected by the central bank-government relationship (i.e.. instrument independence, contract based relationship), while communication includes a broader range of forms. Nonetheless, the transparency index complies approximately with the actual degree of openness of communication.

A closer look would allow us to say that for the time being the CBI is not prevailing in China. The People's Bank of China (PBOC) has multiple objectives requiring coordination and joint efforts with other government agencies. The higher authorities (government, party bodies) not only control the appointments and promotion of PBOC's top officials, but also directly influence monetary policy making. The PBOC has a role of implementing monetary policies, while key decisions such as the setting the M2 growth target, adjustments to benchmark deposit and lending rates, and changes in the legal reserve requirement ratio are made by the State Council. However, the bank obtained increasing autonomy in policy implementation due to its unquestioned expertise. On less important monetary operations, such as daily open market operations, FX intervention, and the provision of liquidity, the PBOC can make decisions by itself. The PBOC is both an executor and to some extent an originator of monetary policy. "The responsibility of PBOC is to advise on the formulation and adjustment of monetary policy and policy targets for a certain period, application of monetary policy instrument, major monetary policy measures and the coordination between monetary policy and other macroeconomic policies" (PBOC web site). The process can be summarized as follows: "PBOC proposes but state council disposes" (He and Laurent), which is also a reason for lagged response of monetary policy as often observed. The State Council is not a homogeneous entity. The decision of the State Council can be better understood as an outcome of policy bargaining between the different departments under the supervision of the State Council. Sometimes the central bank is able to implement its preferred policy, at other times, PBOC's proposals are overruled. The following example illustrates the present situation. The Chinese monetary policy closely watches monetary aggregates. Capital and trade flows directly affect currency reserves and the monetary aggregates. Capital outflows cause a contraction of liquidity while trade surplus increases it. Monetary policy uses reserve requirement changes to set the money supply at the desired level. Lower reserve ratio frees liquidity, while higher ratio absorbs it. Based on the difference between actual and targeted money supply, the central bank makes a recommendation to the government on the reserve requirement ratio setting, however, the final decision remains in the hands of the government. Information on changes in monetary aggregates as well as the expertise to evaluate the economic impact of these changes are fully available at the central bank. In many cases the central bank's recommendations are adopted. This means that the actual role the central bank plays in the conduct of monetary policy is more than what would follow from its formal status. Good persuasive skills of the governor and high professional credibility of some senior managers do have a role to play in this. The PBOC is far from being puppet marionette without any autonomy. Nevertheless, there are nuances to this picture.

The current president is completing his third five-year term in office. However, according to every research on independence, re-appointment is not compatible with the principle of CBI. The possibility and the intention of re-appointment brings into life the motivation to be in compliance with government expectations. This compliance might be in conflict with monetary policy considerations. Therefore, the government may want to appoint someone as head of the central bank who is expected to conduct an accommodative monetary policy.

It follows from the above that instead of being a decision-making body, the "Monetary Policy Committee is a consultative body for the making of monetary policy by the PBC" (PBOC web site). 7 members out of 15 come from government or near-government institutions. In early 2016, the government representatives in the MPC were the Deputy Secretary-General of the State Council, the Deputy Head of the State Development and Reform Commission, the Vice Finance Minister. Besides them the Chairman of CBRC, the Chairman of CSRC, the Chairman of CIRC, the Commissioner of National Bureau of Statistics, and the President of the China Association of Banks were also members of MPC. Those directly or indirectly associated with the government are ex officio members, their appointment does not have a predetermined term. They remain members of the Council as long as they stay in their initial office. Consequently, dismissal rules are not applicable in their case. As a result of its composition, the MPC of PBOC is a tool of enforcement of government will.

The composition of the MPC of the Hungarian central bank is included for comparison. The most striking difference is that no government representative can be found in the Hungarian Council. *(Table 1)*

From the perspective of European banking rules, the presence of active business people at the MPC meetings represents a clear case of conflict of interest. The President of the China Association of Banks who is, at the same time, the chief executive officer of a leading commercial bank gets first hand exclusive information on issues and recommendations discussed at the MPC meetings. Decisions on the operational use of policy instruments may not be made at the MPC meetings. In this way, no commercial bank can gain an immediate competitive advantage. The Council mainly discusses strategic and broader policy issues. The exclusive access to information on these can support the business policy and product development of any commercial bank. Therefore, the insider information on MPC meetings creates unfair competitive advantages.

Table 1

Background of the MPC's external members

China (2016)	Hungary (2009-2011)
7 government official, 1 banking sector, 3 academia	1 academia, 1 industrial sector, 4 consulting business/think-thanks
• Deputy Secretary General of the State • Deputy Hand of the State Development and Reform Commission • Vice Finance Minister • Chairman of CRBS • Chairman of CSRC • Chairman of CIRC • Commissioner of National Bureau of Statistics • President of the China of Association of Banks • Assistant of PBC Governor • 3 experts from the academia	• Head of a consulting company (former chief economic of a commercial bank) • Head of Department of Finance at a Hungarian university, • A senior research fellow of an independent think-thank, former chief economist of the central bank, • A senior research fellow of a research institute, • Former CEO of a major industrial company, • Head of a private Law Office (an expert of legal issues of finance)

Source: own compilation

With regard to monetary financing, the Chinese regulation contains the most up-to-date standards. Article 29 and 30 of the central bank act[3] prohibit crediting the government or purchasing government securities. This regulation has been in force since 1997. It is worth noting that the very same year a very similar regulation was introduced in Hungary.

The Chinese regulation, similarly to the regulation in many other countries, does not exclude the purchase of government papers on the secondary market. However, according to the data, the PBOC does not show any sign of activity on the secondary market. A negligible nominal change of the claims on government and marked growth of assets resulted in a drop of the share of claims on government from 9,6 percent in 2007 to 5 percent in 2013.

Under a special government decision article 30 of the law allows lending to designated non-financial lending institutions. Such placements have not taken place over the past 10 years, the size of the stock is insignificant (0.01 percent of total assets).

3 The People's Bank of China may not make an overdraft for the government, and may not directly subscribe or underwrite State bonds or other government bonds. (Article 29)
The People's Bank of China may not provide loans to the local governments or government departments at various levels, to non-banking institutions, other units or individuals, with the exception of the specific non-banking institutions as decided by the State Council. (Article 30)

Table 2

Selected Assets of the Chinese Monetary Authority 100 M yuan

	2006	2007	2008	2009	2010	2011	2012	2013
Claims on Government	2856	16317	16196	15662	15421	15399	15313	15313
Claims on Non-financial Sectors	66	63	44	44	25	25	25	25
Total Assets	128574	169139	207096	227530	259274	280977	294537	317278

Source: Almanac of China's Finance and Banking, 2014

China has not implemented quantitative easing based on the purchase of State securities. The global financial crisis did not create an emergency situation, forcing out to change the previous practice of monetary financing. The existing regulations and actual practices in line with these represent an achievement that is worth preserving for the future.

The substantial indebtedness and the poor quality of loan portfolios in the local government sector have become a financial stability risk in China. One way to treat these problems is the conversion of local government loans into municipal bonds. According to plans, the newly created bonds would be subscribed by banks which provided the original loans, and local governments would use bond sale revenues to repay their loans. In this way commercial banks can restructure their assets by transforming loans into local government bonds. The rationale for the local government is that bond yields are lower than the interest rates on their loans. This negative gap results in a loss to the banks. The banks' benefit stems from the fact that by using bonds for repo purposes they can get new liquidity. The additional business activity supported by the new liquidity may generate higher profits than the loss produced by the loan-bond transformation. As a result of the repo transactions the local government bonds move to the central bank which seemingly contradicts to the ban on monetary financing. However, the central bank does not have access to these bonds at the primary issue, and even more importantly in the framework of a repo transaction, the central bank does not become the owner of those bonds. Therefore, the loan-bond transformation plan does not seem to violate the ban on monetary financing.

The Chinese central bank's communication practice is still reminiscent of the model of the central banks of the past two or three decades.[4]

4 The next assessment is primarily based on the English language communication channels. In most countries, there is a close to 100 percent congruence between the local language and the English language versions of the central bank's web site. However in China, the English language site seems to fall sharply behind the Chinese one.

Communication is opaque, rare and some of the usual communication channels are non-existent or underutilized in China. The PBOC has no schedule for policy decisions, no published votes or meeting minutes, and no regularly scheduled press conferences. The governor in 2016 spent months without making public comments even after a surprise yuan devaluation causing reactions on global markets.

A specific communication (and a full policy) tool of PBOC is window guidance. Window guidance is often termed as moral suasion is a way to persuade banks and other financial institutions to keep to official guidelines. This is a pressure for 'moral responsibility' to operate in a way that is consistent with furthering the good of the economy. In the case of PBOC, moral suasion or window guidance has been applied to achieve the bank's deposit or loan targets. Such communication is a real monetary policy action through words and not deeds providing market participants with information on unobserved monetary policy decisions. However, an intensification of communication should not mean more window guidance but rather the opposite. Phone calls and informal pressures should be replaced by market (price) signals establishing a more transparent and predictable market environment.

As of today, the Chinese central bank does not have a single macro-economic assessment and prognosis discussed and approved by the executive bodies. In this way, the economic actors cannot rely on a PBOC forecast when they try to anticipate the next moves of the central bank. For this reason, the central bank's actions are hard to predict.

Generally speaking, a central bank's website is a primary channel of communication. It is a key source of information for market actors, analysts, journalists and the wider public as well. The central bank can broadcast messages through this site about its goals, the implementation of its plans and its performance. The PBOC English language website does not meet these requirements. It provides very limited information about the framework and mechanisms of the monetary system. It appears that its maintenance is far from being regular. At the beginning of 2017, the most recent statistics published concerned the year 2010. Published data are sporadic and insufficient.

Central European central banks have various regular publications. These provide detailed explanations on the use of policy instruments; assess macroeconomic processes; publish findings of researches made by the central bank. The Chinese central bank has a much narrower selection of English language publications.

Research publications provide several benefits

- they improve the effectiveness of monetary policy. If the public has a better understanding of policy actions, decisions will come less as a surprise and economic actors will be more likely to make moves in conformity with monetary policy intentions.

- research publications help to build a reputation (credibility) of a prestigious institution where decisions are backed by advanced research work

- they enhance self-fulfillment and career building of junior central bank employees. Publications help to build a personal reputation of the author, opens up new job/ career opportunities which is an important job reward beyond salary

Table 3

Central Bank research publications in CEE countries

Hungary	Poland	Czech Republic	Romania
Working papers: 3-11 article/year	Bank and Credit bimonthly (4 article/vol.) scientific journal	Working papers: 15-16 article/year	Occasional papers: 1-12 article/year
Bulletin 2-4/year with 5-6 article/year	Working papers: 26-33 article/year	Research and Policy Notes: 2-4 article/year	
Occasional papers 2-4 articles/year		Bulletin twice a year, 4-5 articles each month	

Source: central banks' web sites

In China press releases or minutes are not published after the meetings of the MPC. No press conference is held to give information on issues discussed at the meeting. Interviews with senior managers are made on an ad hoc basis, especially when tension in markets occurs. It is noteworthy that only the top leaders communicate, staff members very exceptionally give experts interpretations of policy decisions or economic developments which are of major importance for the monetary policy.

6. The Possible Direction of Change

As China moves towards a more capital market-based financial system and allows capital to flow more freely, communication is winning greater recognition from the management of PBOC. A meaningful development of communication has been a clear determination at PBOC. Improvements are likely to take place in the following areas:

- More frequent public comments/statements/interviews/articles by the top management can be expected.
- The actual large gap between the Chinese and English version of the central bank's website will be tightened substantially.
- More research and more publications are coming in the future. Specific preparations are being made to launch a peer-reviewed Working Paper Series with its own editorial board.[5]

As for the macroeconomic forecast of the PBOC, the author of this article cannot underscore enough the importance of a single PBOC forecast published and discussed with market actors. One commonly accepted forecast instead of competing projections of different units is a condition to the consistency in monetary policy as well. This final PBOC forecast does not have to be the product of one dedicated department. Different units should provide their inputs, they can express their concerns during the preparation phase, but at the end of the day one single forecast should come out under the leadership of a well-chosen department. In this way, a single forecast becomes an output of an integrated effort of many.

If markets are not only aware that PBOC uses its own forecast to back its monetary policy, but they know the forecast itself, then predictability of monetary policy should significantly improve. Therefore, the forecast PBOC uses should be published together with a narrative. Arguments make numbers more credible. They help markets to understand the way central bank thinks. Publication of data and the basics of the model used during the forecasting exercise makes forecasts more persuasive. If these remain unknown to the public the credibility of the forecast will be limited. According to the experience of many countries, central bank forecasts are key instruments in shaping market expectations.[6]

Communication practices related to the MPC's meetings are a function of the future status of the MPC. Reflections about the PBOC's independence is currently at an initial stage, but the three most important fundamental issues have already been addressed. The first: the matter of hierarchy between the multiple objectives of

5 These conclusions derive from the consultations conducted within the PBOC.
6 The fear from publishing the forecast may derive from the harm a wrong forecast can cause to the reputation. This risk should not be overstated. The central bank has a similar or better set of information than anybody else. The quality of central bank forecasts depends on its analytical capacities. Once they are built up, why should the central bank forecast be of inferior quality than those of commercial/investment banks, horribile dictu those of the government? Having said that, we should make clear that forecasts are never fully precise. External shocks are unforeseeable. There is an important difference between forecasting errors and the deviation of forecast figures from actual figures.

the central bank. If the central bank (or the government) decides to set a primary objective (and several secondary and tertiary objectives), the credible commitment to it requires independence. A meaningful and credible primary objective requires the right for the central bank to use monetary policy instruments in an autonomous way. In reality, this is not solely an independence issue. Rethinking the central bank's objectives implies the reformulation of the entire monetary policy regime as well.[7]

The second issue: The MPC should have executive and decision-making powers, and should not be limited to a consultative role. The third issue: a change in the composition of the MPC. The predominance of (near)government members will (or will not) be replaced by that of independent professionals. However, in order to ensure that professional rather than political perspectives prevail, appointment and dismissal rules, regulations regarding terms in office, and conflict of interest rules will have to change accordingly.

The acquisition of decision-making powers for and the change in the composition of the MPC do not have to take place at the same time. A sequential order may ensure a gradual transition from the current state to a more independent one. Any one of these two changes can serve as a first step. One possible scenario is that the decision making rights are delegated to the MPC first without a simultaneous change in its composition. This is a transitory stage towards real independence. The predominance of ex officio members would remain to ensure that no decisions contrary to the government's will are made.

The alternative scenario is the replacement of ex officio members with independent experts first, while the consultative role of the Council remains unchanged. In this case the loss of control over the members of the Council does not necessarily weaken the predominance of the government's will as expert recommendations can be rejected any time (and also the selection of experts is made by the government).

The state of independence will be reached with the second step, namely by the delegation of decision-making rights or through the prevalence of experts in the MPC. The two possible ways are described in the following diagram.

7 Goodfriend-Pasad (2006) make an explicit recommendation to announce an inflation target, which should become a nominal anchor under a flexible exchange rate regime. In addition, they emphasize the importance of operational independence, including control over the central bank's foreign exchange reserves.

Table 4

The state of independence

		Function	
		Consultative role	Decision making power
Composition	Government members *	A	B
	Non-government members	C	D

Source: own compilation
Notes: A – current state B – transition state C – transition state D – target state.

Two possible paths occur: (1) From state A to state B first, then from state B to state D; or (2) from state A to state C first, then from state C to state D. The issues related to PBOC's independence will not be resolved within the competence of the central bank. They are subject to political processes and broader public discussion. Nevertheless, it is very important that the central bank has begun shaping its own vision on the most expedient institutional set-up of monetary policy making.

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Abbreviations

AFTA	ASEAN Free trade Agreement
AIIB	Infrastructure Investment Bank
APEC	Asian Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
BIT	Bilateral Investment Treaty
CEPA	Closer Economic Partnership Arrangement
ECFA	Economic Cooperation Framework Agreement
EU	European Union
FTA	Free Trade Agreement
GCC	The Gulf Cooperation Council – it contains six members (Bahrain, Kuwait, Qatar, Oman, Saudi Arabia, United Arab Emirates)
GVC	Global Value Chains
MES	Market Economy status
PPP	Purchasing Price Parity
PRC	People's Republic of China
RCEP	Regional Comprehensive Economic Partnership (RCEP
RCEP	Regional Comprehensive Economic Partnership, ASEAN+6
RTA	Regional Trade Agreement
TPP	Trans-Pacific Partnership
TTIP	Transatlantic Trade and Investment Partnership
WTO	World Trade Organization