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CHINA'S BRI

Implications for Europe

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China released key details of its Belt and Road Initiative (originally termed "One Belt, One Road"), during President Xi Jinping's visits to Kazakhstan and Indonesia in the Fall of 2013. Initially billed as a network of regional infrastructure projects, encompassing road and rail routes, as well as oil and gas pipelines and facilities (the "Belt"), the scope of the BRI has continued to expand over the past few years. The "Road" component of China's plan, the twenty-first-century Maritime Silk Road, envisaged a network of new port facilities and other coastal infrastructure extending from China through South and Southeast Asia all the way to Africa and the Mediterranean. The initiative featured prominently in China's 13th Five-Year Plan, guiding national investment strategy from 2015 to 2020, and enhancing the coordination of all China's policies across the Asian continent, including financial integration, trade liberalization, people-to-people connectivity, and a "digital silk road." Although the geographical coverage of the BRI has repeatedly expanded, there is one long-lasting trend. Both the overland Silk Road Economic Belt and the Maritime Silk road have fundamentally been linking China with the European continent and its 500-million consumer market.

From a Chinese viewpoint, there are many benefits to multiple interactions with the European Union, which is now China's largest trading partner, but also with countries at the periphery of the EU such as Norway, Iceland, Switzerland, or the Balkan states.

First of all, on the economic front, Beijing is attempting to alleviate its chronic overcapacity by investing in infrastructure along the trade routes to the European continent.

Second, it helps Chinese companies, mainly state-owned enterprises, to develop their experience abroad in fields that are important to China's future: construction, telecommunication, transport, digital technologies.

Third, it allows Beijing to increase its influence in regions where it was relatively weak, including Central Asia and the Middle East while targeting the largest non-US component of "the West," the European Union, a potential partner for a country which officially declared its interest in taking "center stage" in international relations.[1] Under the current US administration of Donald Trump, Sino-American relations reached one of their lowest points in 2019, allowing proponents of a rapprochement between Europe and China to take their chance. In Beijing, the current period is considered extremely favorable to reinforcing Sino-European ties, especially on the economic front. But while US–China relations appear strained, it may also be risky to assume that the Chinese leadership has put aside its fascination/obsession with America, the only remaining superpower it may compare with.

From Chinese FDI to BRI projects: a new era of competition in Europe?

From the early 2000s, China's "going global" policy encouraged Chinese companies, both state-owned and private, to pursue opportunities abroad in order to acquire technologies and expand their footprint, using Chinese state-aid to develop.

Both Europe and the United States attracted major Chinese FDI projects in recent years (overall 90 percent of total FDI between 2000 and 2018). China's annual FDI into the EU skyrocketed from $840 million in 2008 to $42 billion in 2017, covering a wide range of geographic areas and industrial sectors, including automobile, energy, robotics, port and airport infrastructures, telecommunications, hospitality, finance, retail, fashion.[2] The count about doubles when including Switzerland, a non-EU country, which has captured the lion's share of Chinese FDI with ChemChina's acquisition of the agri-business giant Syngenta for $43 billion – the world's single largest acquisition by a Chinese company. However, data from the last two years indicates that in aggregate terms Chinese FDI into Europe is slowing down from its 2016 peak. In 2018, Chinese FDI in Europe declined by 40 percent compared to 2017, for a total of $22.5 billion.[3] The 2017–2018 decline in FDI in Europe is largely the outcome of the Chinese government's recently introduced controls on private capital outflows.

From 2016, the Chinese official language started describing more and more FDI as BRI-related.

In Greece, the acquisition of a Piraeus Port Authority control stake by China Ocean Shipping (Group) Company (COSCO) in 2016 was the result of a long negotiation, which started under the Conservative government which leased two terminals to COSCO for a 35-year period, immediately after the financial crisis. Piraeus – now the world's thirty-sixth commercial port in the world, and with a 51 percent control stake by COSCO – has been described as a successful project "which gives a snapshot of the immense business potential possible through growing trade and connectivity between China and Europe, highlighted by the

Belt and Road Initiative" according to a Chinese official report [4]. President Xi Jinping toured the Greek harbor during his state visit in November 2019. Some €395 billion of Chinese goods were transshipped through the Greek port in 2019, and COSCO's investment has been successful both "in operational and management terms," according to a well-informed local analyst, Plamen Tonchev. On a less positive note, the Chinese investment has not produced a lot of jobs, although it may have saved some. Looking at the distribution of benefits, one should also add that "economic gains are overwhelmingly in favour of China",[5] the same analyst wrote. Meanwhile, some further expansion projects by COSCO have been slowed by local conditions.[6]

Other BRI-related investments in Europe include the "Friendship Bridge" in Belgrade, the Hålogaland Bridge in Norway (built-in cooperation with a Serbian firm, VNG),[7] and the €357-million Croatian bridge across the Mali Ston Bay, which is 85 percent financed by EU structural funds.[8] Meanwhile, the upgrading by Chinese firms of an existing railway line between Belgrade and Budapest appears to have stalled ever since the Hungarian government failed to comply with EU competition rules. The European Commission has been investigating the matter. Although the BRI-enthusiast Serbian government appears willing to start the construction, Chinese contractors have adopted a wait-and-see attitude.[9]

China's BRI support through other means

First and foremost, China has been targeting Central and Eastern European countries through the so-called 16+1 mechanism, a process initiated by Beijing in 2012 to encourage links between China and the region.[10] Many of the countries involved in this project felt chastised by the EU and Germany during the financial crisis and chose to engage with China in order to attract fresh investments (which in fact have not always materialized). From the Chinese side, there are also old ties to be revived between the PRC and some of the former members of the socialist block. The creation of the 16+1 group is a lot more about initiating a network than about actual investments in those countries.

Since Greece officially joined the forum in 2019, the group now has 17 members, including 12 EU member-states, all willing to meet once a year with China's prime minister Li Keqiang and to be part of a coalition of nations friendly to China. China announced the establishment of a €3 billion fund to encourage Chinese investors to engage in public–private partnerships for infrastructure development in the region, as well as in the privatization of a range of industrial enterprises. In conjunction with these efforts, China is exploring investment in maritime port and airport facilities in Bulgaria, Slovenia, and Croatia.

All of these activities are seen as integral parts of the BRI. Twelve members of this 17+1 platform have signed the formal BRI Memorandum of Understanding, although these countries have no correlation with where the growth in volume of Chinese FDI has been happening, nor with the largest destinations of

Chinese capital. In March 2019, during President Xi Jinping's state visit, Italy became the first G7 country to formally endorse the BRI. Luxembourg and Switzerland followed suit in April. Despite the 16+1 initiative, the Central and Eastern European countries made up only 1.5 percent of all the Chinese FDI in the EU in 2018.[11] Overall, it is too early to see many of the promised investments linked to adherence to the BRI, since European countries have only been "joining" the initiative recently.

In Italy, China is working to develop trade hubs on the Adriatic side (to reach Central Europe) and on the western coastline of Italy (to reach France and Spain). The port of Trieste, one of the new investment projects announced during Xi's visit, is part of the EU–China-sanctioned "Trihub" project aimed at increasing reciprocal infrastructure investments, and China Merchants Group began talks in late 2018 to take over shares of the port from its Italian operators (but according to a recent report, talks to acquire shares in the logistics platform of Trieste port are still going on without any official agreement[12]). CCCC, which signed an agreement with the port of Trieste as part of Italy's MoU[13], is similarly exploring a €1.3 billion investment in the port of Venice. In 2018 China Merchants Group had already invested €10 million in the port of Ravenna. But China's largest existing stake in Italy is the Vado Ligure port near Genova, where it owns a 49.9 percent stake (owned by COSCO and Qingdao Port) with a 2016 investment that was planned to be operational at the end of 2019.[14]

Second, China has tried to rally support by organizing thematic conferences and events as part of its "forum diplomacy." That includes the Council Meeting of the Belt and Road News Network (BRNN) which met this year in order to promote "Belt and Road cooperation." [15] China also organized two major Belt and Road Forums (BRF) in Beijing, in 2017 and 2019, in the presence of many foreign dignitaries. In both cases, a number of European leaders attended, including no fewer than ten in 2019 (Italy, Portugal, Austria, Greece, the Czech Republic, Cyprus, Hungary, Luxembourg, Switzerland, Serbia). The European Commission was also represented by one of its commissioners and, in 2017, EC vice-president Jyrki Katainen pointed out that, although China and Europe were at "both ends of the BRI," a number of prerequisites were necessary for the EU to engage further, including "openness, transparency, interoperability, sustainability, and complementarity with other networks."[16]

Policy orientation and European interest in China trade deals and investment

Beijing's new initiatives, including the BRI, have increased competition in Europe as countries appeared to have rushed to sign new trade and investment deals with China.

Western European Countries, in particular, who first competed for a share of China's market in the 1990s, have started competing for a share of its outbound investments.

The United Kingdom's attitude towards China underscores this point. In the 22 years since the British returned Hong Kong to China, London has courted China in a way that has surprised even Beijing. In December 2013, former British Prime Minister David Cameron, accompanied by six ministers, led an impressive 120-member business delegation to China. In September 2014, during a visit to China that took him across the country as far as the western Xinjiang autonomous region, British Chancellor of the Exchequer George Osborne proclaimed a "golden decade" in the Sino-British relationship. The United Kingdom then became the first European country to join the AIIB as a founding member – paving the way for France, Germany, Italy, Poland, and other close US allies to join. The UK is already Europe's top destination for Chinese foreign direct investment, with stocks totaling $55.3 billion in 2018, across sectors from banking, property, and retail, to telecommunications, energy, and utilities. With Brexit looming, it is highly probable the trends will continue. Immediately after taking office, the current Prime Minister Boris Johnson declared he was "enthusiastic about BRI" and that his government would be "pro-China."[17]

Since the start of its open-door policy 41 years ago, China has shown an astute grasp of European politics and an aptitude for playing one European country off against another. The 16+1 initiative is a case in point, but large European countries follow suit. While London has now proclaimed its desire to serve as a bridge between Europe and China[18], Beijing has continued to court other European countries. France was the first Western country to establish full diplomatic relations with the People's Republic of China in 1964. As a permanent member of the UN Security Council and one of the world's top defense spenders, Paris is trying to build a long-term global partnership with Beijing. In order to build a long-term alliance with Xi (and also attract Chinese tourists and investors to France), President Emmanuel Macron made visible gestures to please the Chinese leadership during his November 2019. He was rewarded with some contracts, but Xi then flew to Athens the week after, displaying a message of "deepening cooperation" with the newly-elected Greek government. China understands it is dealing with a divided Europe with diverging interests.[19]

Germany is the second-largest recipient of Chinese FDI in the EU, including machine-tools, semi-conductors, robotics, automobiles, and financial services. In September 2019, the Chinese President welcomed German Chancellor Angela Merkel to China for her 12th official visit since 2005, accompanied by a substantial business delegation focused on concluding large investment and trade deals. Merkel has been hoping to crown her 12 years at the German Chancellery by finalizing an EU–China bilateral investment treaty in Leipzig, but things appear far from certain due to opposition with the German establishment itself.[20]

Other examples of countries courting China at various times include Portugal, which has attracted substantial and diversified Chinese investments;[21] the Czech Republic;[22] and most West Balkan countries.[23] Under Prime Minister Viktor Orban, Hungary has been welcoming Chinese investments even before the BRI launch and made headlines by blocking an EU statement criticizing China's human rights record in 2017, withdrawing from a 2018 joint letter by all 28 EU ambassadors to China questioning the BRI as running "counter to the EU agenda for liberalizing trade", and by "pushing the balance of power in favor of subsidized Chinese companies."[24] In 2016, Greece and Hungary blocked direct criticism by the European Union External Action Service (EEAS) of China's role in the South China Sea following the decision by an international arbitration court in The Hague to strike down Beijing's legal argument.

FDI or BRI?

While the Chinese government has been promoting the BRI towards European countries, the reality is that most Chinese FDI, including by state-owned enterprises[25] has been targeting countries that did not officially join the BRI. Between 2000–2018, the biggest recipients of cumulative Chinese investments were the UK ($55.3billion), Germany ($26.3 billion), Italy ($18billion), and France ($17.5 billion).[26] Of these four, only Italy recently "joined" the BRI.

Figure 8.1 shows that several countries, including Germany, the UK, and France, have continued to attract Chinese FDI despite not being included in the BRI.

There is a long list of European countries who have signed on to the BRI through the formal Memorandum of Understanding, but these countries do not correlate with where the growth in volume of Chinese FDI has been happening, nor with the largest destinations for Chinese capital.

Behind the big picture of an aggregate fall in FDI, there are shaper increases in a more diverse pool of EU countries: Spain, Sweden, Luxembourg, Denmark, as well as Hungary, Croatia, Poland, and Slovenia all saw growing investments, as did two of the more established FDI markets Germany and France.[27] Overall,

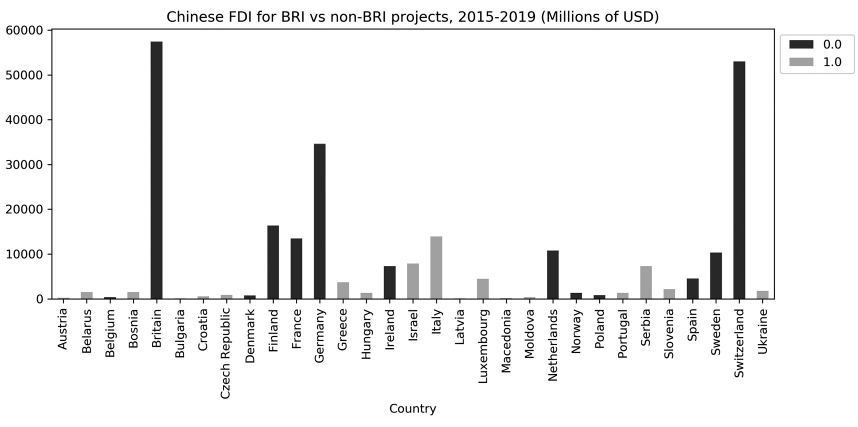

FIGURE 8.1 Chinese FDI for BRI vs. non-BRI projects, 2015–2019 (source: AEI, Chinese FDI tracker, 2019).

Chinese FDI, especially state-backed, has tended to target the strong industries in advanced economies. In Europe, this has been advanced manufacturing industries, with automotive, chemical, agribusiness, energy, and machinery taking a significant share of non-infrastructure (non-greenfield) investment. It is mainly in those countries where infrastructure is weaker and who have a connection to the BRI that China has focused on building up railways and ports to connect its commerce routes. Recently, there were fewer 'mega-deals' and a shift away from infrastructure and real estate projects in favor of more consumer-facing sectors.[28] Investment in utilities and infrastructure went from €13.9 billion in 2017 to €0.5 billion in 2018. The €9 billion takeover bid by China Three Gorges (CTG) for Energias de Portugal SA (EdP) has so far encountered regulatory complications and stalled, but would have otherwise changed this outlook.[29]

Overall, it is fair to say that most European countries do not have strong positive feelings with regard to the BRI.[30] Those which signed MoUs or 16+1 documents labeled as such have done so pragmatically in order to attract more Chinese FDI. It is particularly the case with Greece and Balkan countries, which have attracted most "BRI-labelled investments."

Europe's responses to the BRI

Nevertheless, the continuing expansion of the BRI has created a new set of challenges for Europe. Besides the noticeable intra-European divisions (South/North, East/West), several massive infrastructure projects carry risks of exposing vulnerable economies to potentially unsustainable debt levels. In Europe, the most controversial case has been Montenegro's highway project[31], which has sent the country's debt soaring. Similar questions have been raised about BRI-related investments in Serbia or Albania; in Portugal, a country member of both the EU and NATO, it could be argued that the government's sale of wide-range state assets to Chinese state-owned entities since 2010 has been somewhat overzealous[32] and risked compromising the country's energetic autonomy.[33]

Unlike developing countries, most European states have enough domestic expertise to build or revamp their infrastructure. In addition to European structural funds, institutions such as the European Investment Bank or the European Bank for Reconstruction and Development can provide the funding. In 2015, when outgoing European Commission President Juncker announced a €315bn plan for revamping infrastructure, China expressed some interest but in the end, Brussels and Beijing could not agree on an appropriate frame. Still, unlike most EU countries, West Balkan states – who also happen to have more favorable regulatory environments – are happy to welcome China's help for infrastructure.

How does the BRI impact Europe's economy, internal situation, and foreign relations? The EU has established trade deals with Japan, Canada, South Korea, Vietnam, and Singapore while remaining, at a political level, a close US ally. This explains the cautious approach taken by Brussels when dealing with China's ambitious plan.

Perhaps the most efficient response so far has been the launch by the EU in September 2018 of a new connectivity strategy with the aim of increasing links between Europe and Asia.[34] The strategy seeks to build on and expand existing EU connectivity initiatives by establishing three broad objectives: creating transport links, energy and digital networks, and human connections; offering connectivity partnerships to countries in Asia; and promoting sustainable finance through the use of diverse financial tools. The strategy received unanimous support from European leaders, sending a clear message about the EU's intentions.[35] Early 2019, the EEAS also appointed its ambassador-at-large for connectivity, Romana Vlahutin, who has started promoting related projects. The European Parliament will have to decide how to allocate adequate funding in the upcoming multiannual budget, taping onto the European Fund for Strategic Investments. For its part, the European External Action Service is expected to guarantee €60 billion towards investments in connectivity[36] over 2021–2027, with the expectation that this will help mobilize additional funding from multilateral development banks and the private financial institutions.[37]

Beyond these actions, the EU started in 2019 to re-evaluate its relationship with China, favoring a coordinated EU approach that can effectively stand up to China as an equal power. France's President Emmanuel Macron summoned German Chancellor Angela Merkel and former European Commission President Jean-Claude Juncker to Paris on the occasion of Xi Jinping's state visit in March. For the first time, China's leader faced not just one European counterpart, but three, including the EU representative. Germany's Economy Minister insisted later that large EU member states had "agreed" not to sign similar deals on a bilateral basis, but as a European bloc.[38]

Also in March 2019, the European Commission issued an EU–China "Strategic Outlook" in which it labels China as a "systemic rival" and "strategic competitor" and set out a number of intended steps to contrast the lack of reciprocity and violation of international rules.[39]

> China is, simultaneously, in different policy areas, a cooperation partner with whom the EU has closely aligned objectives, a negotiating partner with whom the EU needs to find a balance of interests, an economic competitor in pursuit of technological leadership, and a systemic rival promoting alternative models of governance,

it says. Such language is unusually bold for the EU and captures the concerns of EU institutions and several member states with an increasingly felt Chinese presence on its soil and periphery.

In addition, the EU concluded the process to introduce a centralized (non-binding) FDI screening mechanism, instructing those eleven EU member-states (out of 28) that still lacked equivalent domestic measures to introduce such provisions aiming at sharing information across the union. Although it specifically targets FDI in infrastructure and technology, this investment screening mechanism is a relatively loose cooperation-and-oversight system. The rapid passing of this new EU measure in just 18 months is indicative of heightened concerns over the terms of China's economic expansion, and the impact it may have on the European economy and social environment.

The 2019 annual EU–China summit, which took place in Beijing in April just before the second Belt and Road Forum and shortly after the announcement of the EU's FDI screening measure, concluded with a stern communiqué and an overall tone not as optimistic as in the past. Issues such as protecting WTO rules including IP protection, avoiding forced transfers of technology, and improving reciprocity with European companies were mentioned. Although these are not directly connected to the BRI, they have a lot to do with China's rise and increasing presence on the European continent. Although Europe's response to China's initiative took some time to develop, it is now gradually taking shape. Between a gradually disengaged US Administration under Donald Trump and an ambitious China with a plan to connect Eurasia as a continent, Europe has no choice but to go on the offensive.

Notes

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