

The potential for growth through Chinese infrastructure investments in Central and South-Eastern Europe along the “Balkan Silk Road”



**Report¹ prepared by Dr Jens Bastian for the
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Executive Summary

President XI Jinping's "One Belt, One Road" or "Belt and Road" initiative, launched in 2013, is a Eurasian grand strategy that seeks to expand and secure maritime routes and road infrastructure networks for China from Asia across Africa to the Middle East and Europe. The blueprint includes a mosaic of trade deals, energy cooperation and financing agreements taking China westwards.

With deep government pockets, growing technical sophistication and a comprehensive investment plan, China's Belt and Road Initiative (BRI) aims to establish the country's political economy on a global scale. In various sectors, it is already achieving dominant status in terms of production, consumption and distribution.

The BRI includes policy initiatives, investment priorities and business decisions by Chinese authorities and companies that can have major impact on countries, regulatory authorities and civil society organisations. Seen from a European perspective, the government-led investment initiatives and lending arrangements originating in Beijing have repercussions in countries as diverse as Germany, Greece, Serbia, FYR Macedonia and Bosnia and Herzegovina.

The rollout of the BRI project in 2013 brought new prominence to China's political and economic agenda. In consequence, its own forms of soft power are now on display along the Balkan Silk Road initiative from Beijing to Athens and connecting with Belgrade, Sarajevo, Skopje, Budapest, Tirana, etc.

With the availability of capital, technology and a master plan under the heading of the BRI, Chinese investments in EU and non-EU member states create leverage for acquisitions and infrastructure innovation on an unprecedented scale. Embarking on a concerted effort, state-owned Chinese banks are providing loans at low interest rates to companies and political authorities in south-eastern Europe. Equally, through the acquisition of ports, opening of bank branches in the region or official lending for bridge building, highway construction and power plant renovation, an infrastructure of transport and logistics networks is being created.

Below-market loans by Chinese state-owned commercial banks to finance new infrastructure capacity is a welcome development for many in countries that are not prime investment destinations or face limitations in terms of private sector lending. But it also raises concerns among critics who question emerging levels of debt dependency on Chinese providers.

China's ambitious BRI project can contribute to help transforming the western Balkans. Seen from the Chinese perspective, their penetration of markets and sectors brings this periphery into a more centrally positioned part of an integrated Eurasian economic zone that Beijing envisions.

The EBRD is engaging with Chinese companies and authorities along the Balkan Silk Road. Tenders have been awarded, and more are expected in the future. This represents opportunities and challenges that will have to be calibrated carefully. The report recommends a pro-active course of action by EBRD offices on the ground.

Table of Contents

Executive summary:	2
1. Introduction: The Balkan Silk Road	4
2. Greece: Bridge Head for China’s BRI to Europe	8
3. Constructing the Balkan Silk Road	13
3.1 FYR Macedonia	16
3.2 Serbia	20
3.3 Bosnia and Herzegovina	25
4. Identifying Spill-over effects of the BRI	32
4.1 Anchor investments creating spill-over effects	35
4.2 Secondary spill-over effects	38
5. Identifying Barriers	41
6. Recommendations for the EBRD	44
7.1 Fostering Policy Dialogue	45
Appendix A: China’s New Silk Road: The Belt and Road Initiative (BRI)	50
A1.1. The priorities of BRI	52
Appendix B: List of Interview Partners in Individual Countries	58
Endnotes	60

1. Introduction: The Balkan Silk Road

President XI Jinping's "One Belt, One Road" or "Belt and Road" initiative, launched in 2013, is a Eurasian grand strategy that seeks to expand and secure maritime routes and road infrastructure networks for China from Asia across Africa to the Middle East and Europe. Beijing's vision of the nature and aims of the Belt and Road Initiative (BRI) include various maritime sections, land bridge connections and transport corridors across various continents. Together, they expand the BRI's geography and thematic content. The geo-economic implications of this orchestrated push from Beijing are potentially vast and long-term. They can shift commercial and geo-economic axes of entire continents.

The *Balkan Silk Road* is the name given to the transport route and logistics corridor China has begun to establish in the Balkan region under the BRI. The Balkans, and by extension south-eastern Europe, is a region where China can empirically test various elements of the BRI. The route starts with the flagship BRI investment into the Greek port of Piraeus, the first major European container port for ships entering the Mediterranean from the Suez Channel.



It is no coincidence that Chinese investments undertaken in large EU member states such as Germany are supplemented by large-scale infrastructure investments in the periphery of south-eastern Europe. The prices for acquisitions are lower while demand for preferential lending conditions is higher in countries along the Balkan Silk Road. Equally, the expansion of Chinese investments towards the Balkan Silk Road is also driven by considerations of human capital

assets in the region. Labour costs in these countries remain low. The relocation or acquisition of manufacturing facilities closer to EU destinations markets may also be influenced by rising labour costs in China.

The first focus of this report is on Greece as a quasi-bridge head being established since 2009 through different port infrastructure investments and logistics initiatives. The “gate towards Europe”, as the Chinese Prime Minister Li Keqiang termed Greece during a visit in 2014, initiates the south-eastern European corridor of the Silk Road. Our roadmap then takes us through the Balkans via the identification of other BRI projects, such as the Belgrade-Budapest high-speed rail and onwards to other EU markets.¹

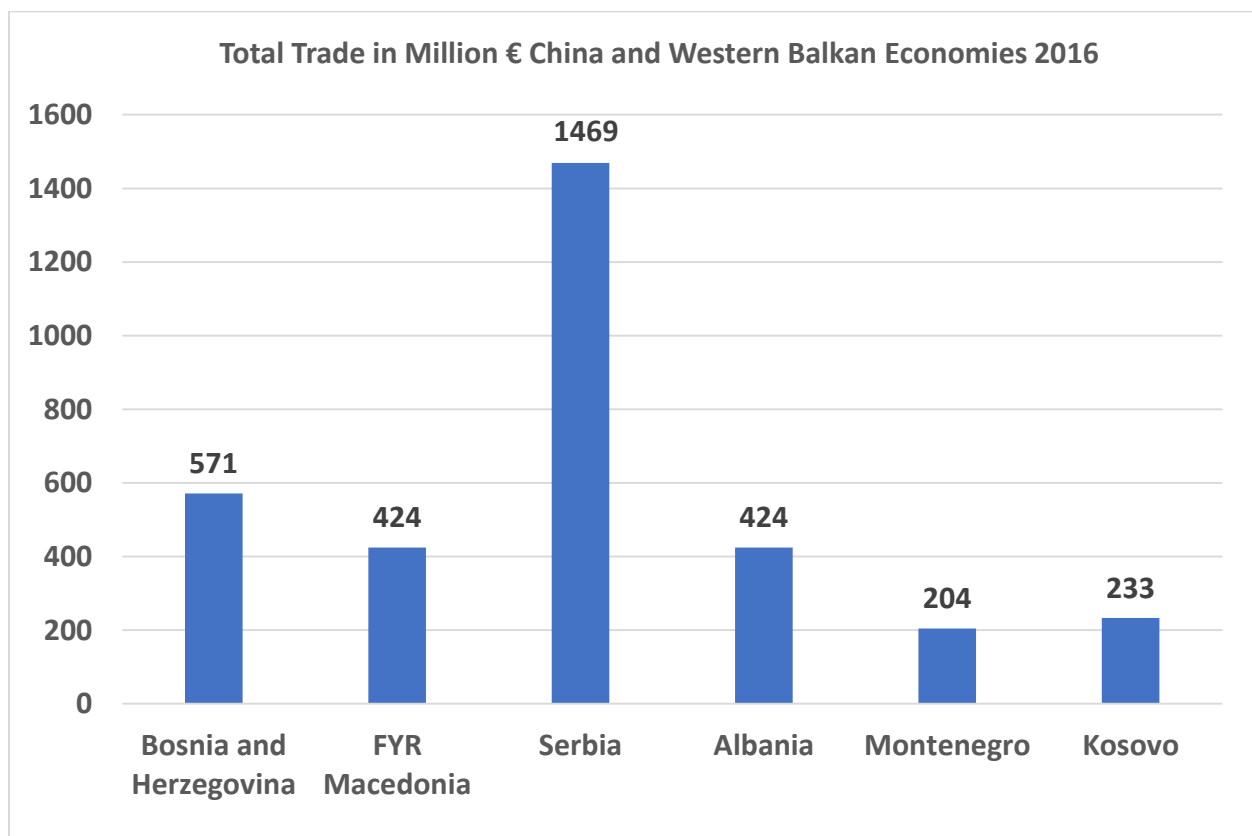
The acquisition of port infrastructure and the subsequent expansion of cargo handling, transport and logistics capacity represents a key starting point in the establishment of transport routes along the European sections of the BRI project. The manner and speed in which such expansion is taking place is impressive, has a strategic logic and is product innovative.

The *Belt and Road Forum for International Cooperation*, which was held in Beijing on May 14-15, 2017, constituted a unique opportunity for countries participating in the Balkan Silk Road project to broaden their economic cooperation with China. Presidents or prime ministers from Russia, Turkey, Greece, Hungary, Poland, Serbia, the Czech Republic, Switzerland, Italy and Spain all participated in the event hosted by Chinese President Xi Jinping. The Forum focused on the coordination of policies, the development of infrastructure projects, the promotion of trade links, and financial sector cooperation. Specific agreements with countries in south-eastern Europe were numerous.²

- At the Forum, the Chinese government signed economic and trade cooperation agreements with the 30 governments, among which are Belarus, Azerbaijan, Georgia, Armenia, Albania, Bosnia and Herzegovina, Montenegro and Serbia.
- The Ministry of Commerce of China signed memoranda of understanding concerning SME cooperation with the Ministry of Industry and Trade of the Czech Republic and the Ministry of Foreign Affairs and Trade of Hungary.
- The Ministry of Agriculture of China signed the Memorandum on Determining the Action Plan on Agricultural Trade and Investment with the Ministry of Agriculture and Environment Protection of Serbia.
- The China Export and Credit Insurance Corporation signed cooperation agreements with the export credit agencies in Belarus and Serbia.
- The Ministry of Education of China signed agreements on education cooperation with the relevant departments in Bosnia and Herzegovina.
- Greek corporate representatives signed an agreement for the construction of a fiber-optic network in the country.

- President-elect Aleksandar Vucic from Serbia held talks about a Sino-Serbian industrial park and negotiations about direct flights between China and Serbia.
- The Export-Import Bank of China signed a loan agreement with the Ministry of Finance of Serbia regarding the modernization of the Hungarian-Serbian Railway Line.
- The Export-Import Bank of China also signed a loan agreement on a telecommunication project with Telekom Srbija of Serbia.

According to data compiled from the European Commission and the Kosovo statistical agency, the total trade volume between China and selected Western Balkan economies reached a level of €3.3 billion in 2015-16. Serbia accounts for almost half of that total trade volume. China's ranking as a trading partner in 2016 after the EU-28 countries was as follows: third in Bosnia and Herzegovina, fourth in FYR Macedonia, fourth in Serbia, second in Albania, third in Montenegro and fourth in Kosovo (for 2015).



Source: Compilation and calculation by the author on the basis of country-specific data provided by the European Commission, Directorate-General for Trade, 29th June 2017, http://ec.europa.eu/trade/policy/countries-and-regions/statistics/index_en.htm.

Data for Kosovo refers to 2015 from the Kosovo statistical agency website: http://askdata.rks-gov.net/PXWeb/pxweb/en/askdata/askdata_External%20trade/?rxid=f81b30b9-6944-42e9-bdfa-726b83f624ee.

Countries like Greece, Hungary, Albania, Montenegro, Serbia, Bosnia and Herzegovina, and FYR Macedonia are making concessions to Chinese investors and lenders precisely because they want China to be embedded in their economies. For countries in the Balkans this embeddedness can also serve as a hedge against Russian and Turkish involvement or present itself as an alternative to EU investment aspirations. It is not so much a binary choice, e.g. between EU and China or Russia and China as seeking additional economic partnerships, free-trade agreements and lending options with Chinese companies, state entities and financial institutions.

Seen in this light, policy makers in Beijing, Tirana, Skopje, Belgrade, Sarajevo, Budapest and Athens frame the narrative as a win-win strategy in the making. They argue that their countries are opening up to China, but that at the same time China is opening up to south-eastern Europe with investments and lending, trade and cultural exchange in various corners of the region.

As countries in the region need to improve their export capacity and attract foreign investment, to the extent that China, Russia, Turkey or Gulf states are willing to provide such resources, Greece, Serbia, Albania, FYR Macedonia, Montenegro, and Hungary will see therein opportunities and choices, while tending to downgrade the perception of risks and dependency.

2. Greece: Bridge Head for China's BRI to Europe

Greece is the point of entry to the Balkan region for Chinese investments under the BRI. The following sections map the development of the infrastructure and logistics sectors along the “Balkan Silk Road” from Greece and up into the Balkans and Central Europe. Apart from the initial maritime focus, Chinese investments in Greece have expanded to other sectors, most prominently tourism and energy.

In recent years, China has moved aggressively to invest in Greece.³ The details of this strategy offer an interesting lens through which to view China's growing capabilities and ambitions in the Balkans and Central Europe. The initial investment in a container port terminal represented a milestone marking Beijing's expanding European ambitions, with major implications over time not only in Piraeus, but equally in neighbouring countries.



The *Piraeus Port Authority* (PPA, Greek acronym *OLP*) is a formerly state-owned company established in 1930. The PPA is the largest company of Greece's port industry and one of the biggest ports in Europe (in terms of container volume turnover). The PPA operates a system of concessions contracts, of which the arrangement for *Piraeus Container Terminal SA* (PCT) is the most important. The port facilities run by PPA are part of the *Trans-European Networks* (TEN-T) and are thus eligible to receive EU financial assistance from the “Connecting Europe” fund.

In November 2008, the Greek government of then Prime Minister K. Karamanlis agreed leased half of the container port from PPA to *China Ocean Shipping Company* (COSCO)⁴ for a 35+5-

year-period. The concessions contract – which became operational in October 2009 - included an upfront payment of €678 million and follow-up infrastructure investments worth €230 million.

From the outset COSCO Hellas, the firm's subsidiary in Greece, expressed interest in plans to buy a majority shareholding in the PPA. In August 2016 COSCO acquired 51 per cent of PPA for the price of €280.5 million (US\$ 312.51 million). The Greek privatization fund *Hellenic Republic Asset Development Fund (HRADF*, Greek acronym *TAIPED*) still holds 23.4 per cent, and other investors 25.86 per cent, of Piraeus Port Authority. The sales agreement stipulates that should Cosco fulfil certain investment conditions up to €300 million in the next five years, it will pay HRADF an additional €88 million and thereby increase its current stake by 16 per cent to a total of 67 per cent.⁵ The total purchase price would then reach €368.5 million for PPA.

Following the purchase agreement Hong Kong-based COSCO embarked on a multi-million investment project to turn the port of Piraeus into a major cruise hub and transshipment logistics centre for travel and trade between Asia and south-eastern Europe. This twofold investment initiative includes the establishment and expansion of logistics bases through COSCO's subsidiary *Piraeus Consolidation & Distribution Center (PCDC)*.

In addition, the new focus on tourism reflects rising demand from Chinese travellers to Greece. As of Autumn 2017, *Air China* will commence direct flights between Beijing and Athens with onward embarkation for Chinese passengers at Piraeus Port onto cruise ships sailing the Aegean, the Adriatic coast and the Mediterranean. Similarly, *COSCO Shipping* signed an agreement with *China Eastern Airlines* in May 2017 for charter flights bringing Chinese tourist groups to Greece.⁶

In February 2017, the *China Development Bank (CDB)* CEO Hu Huaibang announced the lender's intention to expand its presence in Greece, mainly via the financing of infrastructure projects in the energy sector. A memorandum of understanding (MoU) between Greece's central bank and CDB had already been reached in July 2016. The MoU provides for the promotion of bilateral retail and investment banking. CEO Hu noted that CDB – one of the world's biggest development lenders – had created special investment funds for the financing of enterprise development in several European countries.

The MoU provides the financing vehicle for the implementation of a strategic cooperation signed in October 2016 between the *China Machinery Engineering Corporation (CMEC)* and the state-owned *Public Power Corporation (PPC*, Greek acronym *DEH*). CDB would provide up to €1 billion of financing options for infrastructure projects in lignite mining operations conducted by PPC in Greece (e.g. the *Meliti I* project in Florina). The magnitude of the investment project is to serve as a door opener for similar cooperation initiatives between Sino-Greek companies expanding into the energy sectors of neighbouring Balkan countries.

Major Chinese Investments in Greece since 2009

Year	Chinese Company	Greek Company	Sector	Value in Billion €	State of Investment	Nature of Investment
2009	COSCO	PPA	Transport Ports	0.678	Completed	Concessions Contract
2014	China Development Bank	Costa Mare	Transport Container Shipping	1.1	Completed	Official Lending
2014	Export-Import Bank	Thenamaris Ocean bulk	Transport Container Shipping	0.340	Completed	Shipping Infrastructure
2014	ICBC	Libra Diana Shipping	Transport Container Shipping	0.490	Completed	Shipping Infrastructure
2014	China National Aero Technology	Veritas Ship Management	Transport Container Shipping	0.158	Completed	Shipping Logistics
2015	ICBC – Sinohydro	Terna Energy	Energy	0.880	MoU	Energy Generation
2016	COSCO	PPA	Transport Ports	0.280.5	Completed	Majority Shareholding
2017	State Grid Corp. of China	Independent Power Transmission Operator (ADMIE)	Energy / Electricity	0.320	First stage completed Ongoing	24% Shareholding (Right to acquire 66% majority)
Total				4.247		

Source: Author's compilation based on company reporting since 2009.

It should be borne in mind that the Chinese investment in Greece is not only the result of carefully executed economic diplomacy for which the ground work was prepared years before in Piraeus. In December 2016 China's *State Grid Corporation*, the world's biggest utility, purchased a minority stake (24 per cent) in Greece's power grid operator ADMIE. This constituted China's second major investment in Greece in the course of 2016, after the acquisition of PPA.

ADMIE was a fully-owned subsidiary of PPC that is subject to privatisation requirements on the basis of Greece's third macro-economic adjustment programme in August 2015, which is due to expire in August 2018. Put otherwise, China is pro-actively participating in privatization projects as mandated by international creditors in current or former so-called 'programme countries'.

To illustrate: The minority stake investment in Greece supplements equity funding by State Grid Corp. in Portugal (25 per cent shareholding in *REN* in 2012), Italy (35 per cent shareholding in *CDP Reti* in 2017) and Spain (bidding for German utility *E.ON*'s northern Spanish grid).

This equity funding creates a network or cluster of investments that enables State Grid Corp. to gradually establish a regional electricity grid portfolio in Europe. This development is all the more remarkable since it is China-led and contrasts with the low level of cross-border grid investments across the EU by European companies.

Greece's International Trade in Goods with China (in € billion) 2013 - 2015

	Exports	Imports	Balance
2013	0.419	2.19	-1.78
2014	0.279	2.49	-2.21
2015	0.271	2.87	-2.67

Sources: For 2013 and 2014 data: Eurostat newsrelease: 116/2015 26. June 2015 <http://ec.europa.eu/eurostat/documents/2995521/6893875/6-26062015-AP-EN.pdf/44d4c87c-98dd-4061-bdf6-b292884a5073>. For 2015 data see: <http://atlas.media.mit.edu/en/profile/country/grc/>.

The value of imports from China to Greece is steadily increasing while exports are declining. As of end-2015, the total value of bilateral trade surpassed €3 billion. The trade balance is heavily tilted in favour of China. Placed in a regional context, Sino-Hellenic trade volumes are twice as large as China's largest trading partner in the Western Balkans, i.e. Serbia.

The largest trade and manufacturing fair of Greece, traditionally held in the second largest Greek city of Thessaloniki, will host China as the honorary country during the 2017 exhibition (from 09. to 17. September). It marks 45 years since Greece and China launched diplomatic relations.

Unlike other potentially interested parties, China has the financial capacity, the risk appetite and a long-term investment strategy in Greece. It has equally established a credible track record vis-à-vis the Greek political authorities and the business community in Athens. It is now in a first-mover position, submitting binding offers for projects which stand a high chance of being accepted.

As is increasingly becoming clear, the initial Piraeus investment served the purpose of an anchor investment that subsequently started to attract follow-up investment in sectors beyond maritime ports and container shipping. This ‘anchoring’ process is at the initial stages of realization. In the context of the BRI strategy for Greece, the priority sectors will continue to be (port) transport infrastructure, logistics and energy. But these sectors are starting to attract new Chinese investment groups such as *Dalian Wanda Group Co.* or *Greenland Holdings Corp.* which are scanning other sectors, e.g. targeting tourism, commercial real estate, insurance companies and banking services in Greece and beyond.

3. Constructing the Balkan Silk Road

The following sections seek to deepen our understanding of equity funding and debt financing across central and south-eastern Europe (CSEE). This will first involve an analysis of the pipeline of Chinese BRI projects in selected countries along the “Balkan Silk Road”. In a second step the inquiry will discuss existing obstacles and how they could be overcome in order to achieve mutually beneficial outcomes for countries participating in the Balkan Silk Road.

The level of engagement by Chinese state-owned companies, political leaders, diplomatic representations, lending institutions, universities and cultural organisations in central, eastern and southeast Europe is gradually redefining the relationships between China and these regions of the European continent. In particular in countries comprising the Balkans, China is identifying opportunities, while various EU member states currently regard the region primarily through the prism of political instability, refugees and migration as well as the threat of terrorism and drug trafficking.

By contrast, China is establishing new institutional settings for cooperation. Under the umbrella of the BRI exists the “16+1” initiative. The 16+1 framework seeks to improve trade and economic relations between China and 16 countries in Central and Eastern Europe, inclusive of south-eastern Europe. The participating countries are Albania, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, FYR Macedonia, Montenegro, Poland, Romania, Serbia, the Slovak Republic and Slovenia.

The first 16+1 summit was held in 2012 in Warsaw, Poland. Since then, four further summits have been held in Bucharest (2013), Belgrade (2014), Suzhou (2015) and in Riga (2016). These summits are embedded in the *Cooperation between China and Central and Eastern European Countries* organisation, whose secretariat is located in Beijing (<http://www.china-ceec.org/eng/>).

On the summit occasion in 2012, the Chinese government delegation proposed the establishment of the *China-CEE Investment Cooperation Fund* (<http://china-ceefund.com/>). A year later it became operational. The Fund is registered in Luxemburg. Its two main investors are Chinese: (i) *Export Import Bank of China* (US\$ 470 million), and (ii) *Exim Bank Hungary* (US\$ 30 million).

In November 2016, a second Sino – CEE Investment Cooperation Fund was launched with a total volume of USD 11 billion. *Industrial and Commercial Bank of China* (ICBC) is the main funding contributor. The fund will be run by *Sino-CEE Financial Holdings Ltd*, a subsidiary of ICBC). The fund was formally launched by Premier Li Keqiang during his visit to Riga on the occasion of the fifth *Cooperation between China and Central and Eastern European Countries* summit. The fund seeks to raise 50 billion euros in project finance for sectors such as infrastructure, high-tech manufacturing and consumer goods.⁷

The first of these two funds established *CEE Equity Partners Ltd.*, its investment advisory arm (<http://cee-equity.com/>). Some of its most recent activities have been an investment by the Fund in *Javna Razsvetljiva d.d.* and *JRS d.d.* The two companies are market leaders in design and implementation of public lighting and signalling solutions in Slovenia. In January 2017, the Fund

acquired a majority shareholding in both companies through a combination of capital injection and the buy-out of existing shareholders. A second acquisition concerned the *Invitel Group*, one of the leading players in the Hungarian telecommunications market (March 2017).

For countries participating in the 16+1 framework, Chinese capital and infrastructure projects represent a tempting market proposition and “a potential platform for China to leverage its growing economic and political influence with the EU as a whole.”⁸ According to data from the *Chinese Academy of Sciences* (CAS), China’s outward foreign direct investments into the 16 participating countries increased from US\$ 400 million in 2009 to roughly US\$ 3 billion in 2016. The geographical concentration is noteworthy. According to CAS, Bulgaria, the Czech Republic, Hungary, Poland, Romania and Slovakia represented 95 per cent of total Chinese FDI within the 16+1 framework in 2016.

The example cited earlier of *COSCO* investing in the Port of Piraeus in Greece forms part of a larger strategic investment drive across CSEE and the Mediterranean. Apart from Piraeus, *COSCO* has invested in port infrastructure in Albania, Montenegro, Israel, Turkey and Egypt. In 2016, it acquired a 35 per cent stake in the Rotterdam *Euromax-Terminal*.⁹ A similar strategic positioning within southern Europe can be observed by the *State Grid Corporation* of China, with minority investments in grid operators in Greece, Portugal, Italy and possibly Spain.

- What the *COSCO* and *State Grid* investment drives illustrate, is the systematic, strategically driven construction of sector-specific portfolios and linking up their assets across a larger region, i.e. the Mediterranean. The BRI is under construction along the Balkan Silk Road, with a special emphasis on the transport sector and energy connectivity.
 - The former concentrates on supporting shipping routes, port accessibility, road and rail infrastructure logistics and the distribution links of Chinese goods.
 - The latter establishes a regional power network portfolio based on opportunities emerging from privatisations in southern euro zone members that are current or former so-called ‘programme countries’.

Such targeted, sectoral investment and strategic positioning becomes all the more comprehensible when taking into consideration that the 16 countries represent a collective population of over 100 million citizens. In many of these countries, in particular EU and Euro area members, per capita income levels are gradually rising for many working constituents of society. In short, there are manifest new consumer market opportunities presenting themselves to Chinese investors in the medium- to longer-term within the 16+1 framework of economic cooperation.

There are legitimate concerns about the Chinese engagement in the 16+1 framework. These chiefly focus on the following policy areas:

- Chinese companies employ few locals;
- Chinese companies serve as proxies for the Chinese state;
- The infrastructure projects and lending agreements burden governments with large debt obligations.

The emerging Sino-Balkans relationship is a work in progress. The destinations for Chinese investments and lending in the region are multi-layered and proliferating over time into other areas and sectors. The beneficiary countries pursue state-led economic development, a focus that pairs well with Chinese ambitions and mode of implementation.

From the Balkan's perspective, China presents risks and opportunities, be it in lending, engineering capacity or infrastructure development. While the risks are not ignored by decision-makers, they do not take centre stage. Instead, the mixture of risks and opportunities is placed in a narrative of choices and alternatives that Chinese activities offer.

For governments in the Balkans, and by extension in southeast Europe, that lack sizeable foreign direct investment, complain about unproductive relationships with foreign donors and confront obstacles regarding access to finance, the choice of finding alternatives with Chinese counterparties is tempting and potentially promising. While the strategic rational should not be ignored, the behavior of political authorities in southeast Europe vis-à-vis China is also driven by opportunistic considerations.

3.1. FYR Macedonia

In one major respect, FYR Macedonia is an outlier in the Chinese investment and economic cooperation strategy. Back in the early 1990s, the political authorities in Skopje sought international recognition for their country while the so-called 'name recognition dispute' with Greece was escalating. One means to achieve this objective was to simultaneously recognize Taiwan, which in turn was prepared to provide considerable financial resources to FYR Macedonia. This strategy was later abandoned by successive governments in Skopje in favour of a gradual rapprochement with China.

FYR Macedonia: Top Trading Partners 2016 (total goods)

	Partner / Ranking	Value Mil. €	% World
Imports:	EU 28	3,780	61.4
	Serbia	489	7.9
	China	381	6.2
	Turkey	316	5.1
Exports:	EU 28	3,456	69.6
	Kosovo	669	13.5
	Serbia	383	7.7
	Bosnia and Herzegovina	74	1.5
	9. China	43	0.9
Total Trade:	EU 28	7,240	65.0
	Serbia	872	7.8
	Kosovo	698	6.3
	China	424	3.8

Source: European Commission, Directorate-General for Trade, 03.05.2017, http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113381.pdf.

The most recently available international trade data for FYR Macedonia illustrates that China was the country's fourth largest trading partner in 2016 (treating the EU-28 as one partner), reaching a total of €424 million. The trade balance is almost exclusively tilted in favour of China, which is FYR Macedonia's third largest import originator, while it features in ninth position as FYR Macedonia's export destination.¹⁰

Major Chinese Investments and Lending in FYR Macedonia since 2006

Year	Chinese Company	Sector	Value in Million €	State of Investment	Nature of Investment
2006	China International Water and Electric Corp.	Energy	Not available	Completed	TP Kozjak Hydro Power Plant
2010	Zhengzhou Yutong Group	Public transport	Not available	Completed	Supply of double-decker buses for Skopje
2014	Sinohydro Corp. Exim Bank	Motorway Construction 110 KM	574	Ongoing Completion for end-2017	Lending / Construction Kicevo – Ohrid Miladinovci – Stip
2014	China Railway Rolling Stock Corp.	Railway	50 EBRD secured loan	Completed	Electrical trains Railway modernisation
2017	China Railway Rolling Stock Corp.	Electric locomotives	Not available	Ongoing	Supplementary investment to 2014
Total			640		

Source: Author's compilation based on publically available documents and interviews with country representatives.

As a land-locked country in the Western Balkans, FYR Macedonia presents specific challenges for enhanced economic activities by Chinese companies. As maritime considerations can be excluded, terrestrial infrastructure projects are the main priority. Thus, the focus is on establishing branches of logistical corridors in sectors such as energy, motorways and railway modernization.

These corridors seek to connect FYR Macedonia with wider corridor initiatives along the Balkan Silk Road initiative. Seen from this perspective, the limited Chinese investment in FYR Macedonia nevertheless has a strategic focus. The country represents one of the connecting links between port facilities being expanded or acquired in neighbouring countries and transport infrastructure projects. Sino-FYR Macedonian economic cooperation dates back a decade when the first major project was realized in the energy sector.

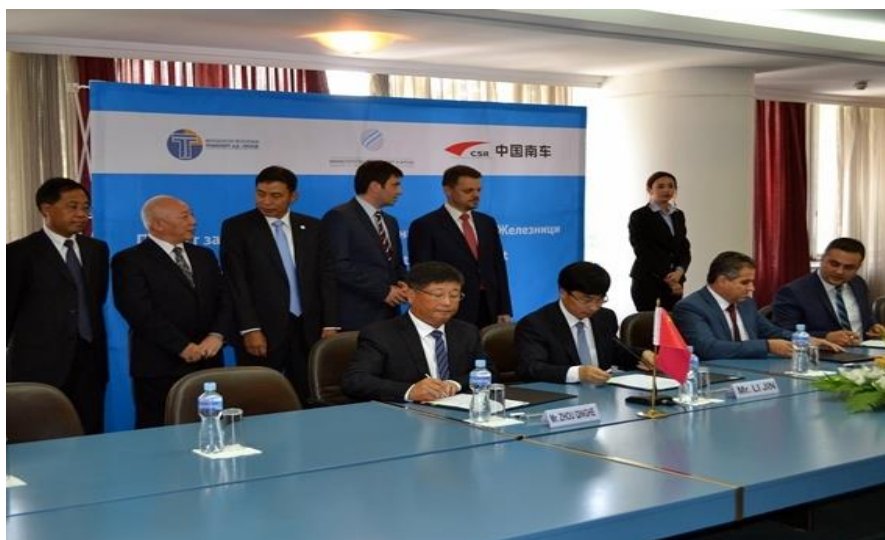
Subsequent infrastructure projects have focused on road construction and railway modernization. These projects form part of regional, rather than country-specific initiatives that Chinese companies and banks are supporting. Railway modernization in FYR Macedonia is a result of the agreements between Hungary, Serbia and China along the Budapest – Belgrade Corridor X initiative.

When driving from the Greek-FYR Macedonia border crossing of Bogorodica near Gevgelija to the capital city Skopje, the construction sites of the A2/A3 highway from Kicevo to Ohrid (57km) and the Miladinovci to Stip motorway are easily identifiable.

Financed through lending by *Exim Bank*, the two infrastructure projects are being built by *Sinohydro Corporation*. *Granit* and *Beton* from FYR Macedonia perform much of the road work as subcontractors. The Miladinovci to Stip highway will dramatically reduce travel time from the capital Skopje to Stip, which is the largest city in the eastern region of the country.

Launched in March and June 2014 respectively, the two projects are expected to be completed by end-2017. They form part of a larger programme to build a European corridor 8, East - West throughout FYR Macedonia. They would thus provide an East-West highway corridor that supplements the South-North corridor that was financed by the EU *European Agency for Reconstruction* in early 2002.

In other more administrative related areas, bilateral cooperation is also advancing. To illustrate, in June 2016 in Skopje, a bilateral meeting took place between the customs administrations of FYR Macedonia and the People's Republic of China. The aim of the meeting was to strengthen the cooperation between the two customs services, established under the *Framework Agreement on Cooperation in Facilitating Customs Clearance* among the Chinese, Hungarian, Serbian and Macedonian Customs, signed in December 2014.¹¹



Signing of the loan agreement for the train project in Skopje in May 2014

The EBRD is engaged in Sino-FYR Macedonia economic cooperation since 2014. The purchase of four diesel and two electric trains by the government in Skopje from the Chinese company *CSR Corporation* was financed by a €50 million loan secured by the EBRD.

The Chinese CSR Corp. was awarded the tender after beating the Swiss train manufacturer *Stadler*. This investment was the second large procurement of transportation vehicles awarded to a company from China. In 2010 China's *Zhengzhou Yutong Group* was chosen to supply the capital city Skopje with 202 retro-looking double-decker buses for its public transport system.

3.2. Serbia

China's economic cooperation with Serbia has expanded significantly since the signing of a strategic partnership agreement in 2009. The bilateral cooperation agreement included infrastructure investments. Primarily project-based on the transport sector, the partnership received extensive state-to-state funding from a variety of state-owned Chinese banks. The third China-Balkans Summit under the 16+1 umbrella was held in Belgrade in December 2014.

Serbia: Top Trading Partners 2016 (total goods)

	Partner / Ranking	Value Mil. €	% World
Imports:	EU 28	10,944	63.7
	China	1,447	8.4
	Russia	1,277	7.4
	Turkey	581	3.4
Exports:	China does not	feature among	top ten
Total Trade:	EU 28	19,865	64.9
	Russia	1,970	6.4
	Bosnia and Herzegovina	1,531	5,0
	China	1,469	4.8

Source: European Commission, Directorate-General for Trade, 03.05.2017, http://trade.ec.europa.eu/doclib/docs/2008/august/tradoc_140028.pdf.

The most recently available international trade data for Serbia illustrates that China was the country's fourth largest trading partner in 2016, reaching a total of €1,469 billion. The trade balance is almost exclusively tilted in favour of China, which is Serbia's second largest import originator, while it does not feature in the top ten positions as Serbia's export destination.¹²

Seen from a Chinese perspective, the Serbian market is rather small and it is a land-locked country. But it is not size nor geography that matter. Connectivity is the underlying issue. Serbia is an attractive partner since it has trade agreements with the EU, Turkey and Russia. It also

enjoys a level of political stability that is not a given in neighbouring countries. Equally, both countries have established a visa free regime effective since January 2017.

The share of Chinese investment (Hong Kong included) in total FDI to Serbia was 3.1 per cent in 2015 and rose to 9.2 per cent in 2016. This considerable increase is primarily attributed to the acquisition of the steel mill *Zelezara Smederevo* by China's *He Steel Group* for €46 million in 2016 (see below). It must also be underlined that a major source of lending by Chinese banks is carried out from Hong Kong, less so from mainland China. According to EBRD estimates, US\$ 350 million in lending during 2015-16 arrived from Hong Kong to Serbia.



Guoli Tian, chairman of the Bank of China, shakes hands with Serbian President Tomislav Nikolic on the occasion of the branch opening in January 2017. Photo: Beta

In January 2017, the *Bank of China* (BoC) opened its new branch in Belgrade. It is a subsidiary of the fully licensed BoC bank located in Hungary. BoC has a strategic partnership pact with the Hungarian authorities since January 2017. This form of indirect investment should for the time being be seen as a political decision in which a Chinese bank establishes a representation in Serbia, only gradually building up its financial operations in the medium-term.

The primary focus is on serving client demands from Chinese and Serbian companies. The bank's chairman, Guoli Tian explicitly positioned the new branch as contributing to China's "One Belt, One Road" initiative. Strengthening its financial sector presence in Serbia and establishing a banking hub for other clients in the region reflects the latest effort by China to move its BRI forward.¹³

However, it has to be underlined that the new branch currently has neither the capital nor the management capacity to finance projects in Serbia. It is not (yet) a deposit taking branch and has not extended any loans to private households or businesses.

Major Chinese Investments and Lending in Serbia since 2008

Year	Chinese Company	Sector	Value in Million €	State of Investment	Nature of Investment
2008	Official Lending	Retail	32	Completed	Belmax Trade Center
2011	Wolong Group	Motors and control systems	Not available	Completed	Sever Company
2012 2014	Official Lending	Energy	293 608	Ongoing	Thermal Power Plant at Kostolac
2014	Official Lending	Mihajlo Pupin Bridge over Danube	260	Completed	Bridge Building
2015	Mei Ta Industrial	Auto Industry	60	Completed	Obrenovac
2016	Official Lending	Construction Corridor 11	350	Ongoing	Cross Border Highway Construction
2016	He Steel Group Investment	Steel Smederevo	46	Ongoing	Modernisation Investment
2016	Official Lending	Rail Reconstruction	Over one Billion	Ongoing	Fast Rail link Belgrade – Budapest
2017	Bank of China	Banking	Not available	Completed	Greenfield investment Branch network
Total			2,661		

Source: Author's compilation based on publically available documents and interviews with country representatives.

Serbia's importance to China's BRI has repeatedly been emphasized by Chinese President XI Jinping, most recently during his three-day state visit in June 2016. XI sees Serbia playing a leading role in the cooperation between China and the countries of Central and Eastern Europe. Seeking to back up such diplomatic statements, Beijing is in the process of becoming a major lender for infrastructure projects in Serbia.

The focus rests on the transport sector, i.e. roads and railways, the steel industry and energy projects (see the table above). In November 2016 both countries also signed an agreement on the mutual abolition of visas. To date, the only Chinese acquisition of a major Serbian company took place in the energy sector. The steel mill *Zelezara Smederevo* is being sold to China's *He Steel Group* for €46 million.

The level of bilateral economic cooperation is further exemplified by two new project proposals. Construction, Transportation and Infrastructure Minister Zorana Mihajlovic met with a delegation of *China Road and Bridge Corporation* (CRBC) in April 2017 to discuss a project to build a 45.4-kilometer road between Novi Sad and Ruma, the so-called Fruska Gora Corridor, which will entail building a Mt. Fruska Gora tunnel. The Serbian authorities are also considering an irrigation tunnel that would be built alongside the road, to link the Danube river and Vojvodina's district of Srem. The Novi Sad-Ruma road will be part of a route that runs to Sabac, Loznica, and the border with Bosnia and Herzegovina, linking Serbia with Croatia and Bosnia and Herzegovina.

At the municipal level, the mayors from Belgrade and Shanghai signed an MoU for the construction of a metro in the Serbian capital in April 2017. The Belgrade Mayor Sinisa Mali said that the project would start within two years. The MoU also includes extending the cities' cooperation in fields such as economy, education, culture, sports, environmental protection, and tourism. Belgrade also plans to buy 80 electric buses, after recently procuring five, from Chinese companies.

The most important form of economic cooperation concerns Chinese lending for Serbian infrastructure projects. According to the IMF resident representative office in Belgrade, the disbursed amount since 2014 is €425 million. This volume is mostly related to loans for highways and power plant investments. This amount would be higher if bilateral loans are included that have yet to be ratified.

This lending activity has two aspects. On the macro-economic side, capital inflows, e.g. in the form of foreign direct investments (including from China), are seen as positive indicators concerning the openness of Serbia for doing business. But capital inflows from Chinese state-owned banks structured as concessional loans for infrastructure projects can also be a matter of concern. It is currently not known how high the share of this lending is when awarded for projects without a public tender.

Two major examples of Sino-Serbian loan agreements that circumvent public procurement processes concern the aforementioned Belgrade – Budapest railway project and the completed

Mihajlo Pupin Bridge reconstruction over the Danube in Belgrade. It is a matter of debate among (international) observers in Belgrade, if a formal tender process would make high-profile infrastructure projects cheaper or not.

The diversity and volume of Chinese investments and lending in Serbia is therefore not without its critics. The degree to which Serbia benefits from its expanding economic cooperation with China depends on an assessment of whether the focus rests too much on loans for infrastructure projects instead of direct investments. The rising trade imbalance illustrates that Chinese companies are increasing exports to Serbia while state-owned banks provide infrastructure lending at preferential rates.¹⁴

Such credit-based economic cooperation is supplemented by many of the construction works currently under way being conducted by Chinese companies. To illustrate the Chinese approach, consider the following: the construction of the Friendship Bridge over the Danube in Belgrade in 2010 was carried out by the Chinese state-owned enterprise *China Road and Bridge Corporation*. The loan for the USD 260 million investment was provided by the *Export-Import Bank of China*.

It is noteworthy that the EBRD has awarded two tenders to Chinese companies in Serbia in 2016. One tender is in rail reconstruction with a CCRC. The other concerns a hydro power plant turbine. The Belgrade Airport concession tender process is currently underway. Four consortia and one company have advanced to the second round where binding offers have to be submitted. China's *Hainan Air Travel Service* and *China National Aero Technology* have been chosen to advance to the second round of the tender for a 25-year concession license to operate Belgrade's Nikola Tesla Airport, the largest in the Balkan region.

These examples illustrate that gradually a project relationship is emerging between the EBRD and Chinese companies. The opportunity to do so in public tenders underlines the willingness of both sides to cooperate with each other, e.g. by testing the waters how EBRD procurement rules are adhered to by Chinese counterparties. There are lessons to be learned from these initial experiences for the future relationship between EBRD offices along the Balkan Silk Road and Chinese companies (see chapter 5).

3.3 Bosnia and Herzegovina

Bosnia and Herzegovina (BiH) does not yet feature prominently on the radar of Chinese economic activities in south-eastern Europe. Foreign direct investment (FDI) has come from Russia in the energy sector. Gulf states have started to invest in real estate and shopping centres. Turkish FDI is mainly concentrated in SME activities.

Nevertheless, the volume of finance in play – committed or offered – from China could be considered substantial. If indeed agreed and implemented – and this is a rather big if – then the total sum would be exceeding €2 billion. Outright acquisitions have not yet taken place by any Chinese companies. The core of their activities is concessional lending and participation in joint infrastructure projects, mainly in the energy sector and prospective motorway construction.

The Political and Administrative Structure of Bosnia and Herzegovina (May 2017)



It is therefore necessary to distinguish between intended or reported (by BiH media) investments on the one side, and the real but limited economic activities of Chinese companies in the country on the other side. A major obstacle for the realization of further projects rests in the complex and

time-consuming political and administrative structure of the country, its entities and (in the Federation entity) its cantons (see the overview on the previous page).

The most recently available international trade data for Bosnia and Herzegovina illustrates that China was the country's third largest trading partner in 2016, reaching a total of €571 million. The trade balance is almost exclusively tilted in favour of China, which is Bosnia and Herzegovina's third largest import originator, while it does not feature in the top ten of Bosnia's export destinations.¹⁵

Bosnia and Herzegovina: Top Trading Partners 2016 (total goods)

	Partner / Ranking	Value Mil. €	% World
Imports:	EU 28	5,068	61.4
	Serbia	928	11.2
	China	558	6.8
	Russia	362	4.4
Exports:	China does not	feature among	top ten
Total Trade:	EU 28	8,499	66.4
	Serbia	1,345	10.5
	China	571	4.5
	Turkey	554	4.3

Source: European Commission, Directorate-General for Trade, 03.05.2017, http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113358.pdf.

Lending flows from China to Bosnia and Herzegovina are geographically concentrated. So far, two projects are located in the smaller Bosnian Entity, Republika Srpska (RS), and two in the Federation of B&H. While the latter two focus on thermal power, the former two concern motorway construction and a thermal power plant.

Major Chinese Investments in Bosnia and Herzegovina since 2009*

Year	Chinese Company	Company / Authority	Sector	Value in Mil. €	Nature of Investment	State of Investment
2014 – 2017	Gezhouba Group + Guandong Electric Power Design Institute	Elektroprivreda BiH (EPBBiH) Tuzla (TPP)	Thermal power plant Energy	722	15% co-financing by EPBBiH 85 % loan from Exim Bank	Framework agreement Lending agreement Seeking loan guarantee
2015	Sinohydro Eximbank	Autoputevi Republic of Srpska (RS)	Transport	600	Motorway construction + Lending	Planning stage
2015	China Development Bank + Dog fang Electric Corporation	Stanari EFT Doboj, RS	Energy	350	Official Lending + Construction of thermal power plant	Completed
2015	Dongfang Electric Corp. Industrial and Commercial Bank of China (ICBC)	Banovici	Energy	388	Thermal power plant Coal mine operation	Tender process ongoing
Total				350		

Source: Author's compilation based on publically available documents and interviews with country representatives.

* The list includes both entities of Bosnia and Herzegovina. The total investment volume only refers to completed projects.

In Bosnia and Herzegovina we can observe a disconnect between what Chinese companies and banks are considering doing on the ground in BiH and what various representatives in the media, political establishment and business community of the country would want to present as agreed Chinese investments and/or lending activities.

To illustrate: the motorway operator *Autoputevi Republike Srpske* in the Bosnian-Serb entity Republika Srpska (RS) claims to have signed a preliminary agreement with the Chinese firm *Sinohydro* for the construction of a 93 KM long section of a 186 KM long motorway linking the Entity's capital of Banja Luka with Croatia's Adriatic city of Split. But according to various observers on the ground, this is a "dream" of the Entity's president, Milorad Dodik, entirely driven by "political considerations".

Traffic-wise, it is not seen as making much sense, apart from the logistical and geographical challenges of building such a stretch of motorway through very mountainous terrain. There are also doubts about the fiscal capacity of RS to finance such an infrastructure project, the cost of which will allegedly reach €600 million. What is clear, nevertheless, is that there are no sovereign guarantees forthcoming from the state of BiH for the Entity's project.

This absence of a sovereign credit guarantee at the state level cannot be compensated for by RS resources. Equally, no Chinese bank would currently be prepared to extend such a credit line to the authorities in RS without sovereign state guarantees for repayment obligations in case of delays or defaults. In the state structure of BiH, such guarantees are frequently extended to infrastructure projects (including to EBRD co-financed projects) and the waterfall structure of repayment obligations in BiH revenue streams prioritizes multi-lateral lenders when it comes to getting repaid on time and in full.

A second proposal in the project pipeline concerns the *Banovici thermal power plant*. The project is reported to have been subject to a qualifying and final tender process in which three Chinese companies participated directly and a fourth indirectly via a consortium led by Spain's *Abengoa SA*. There is currently no timetable for any final decision on the tender.

- The project is being led by the state-run coal mine operator Banovici. However, the operator has never built, let alone operated, a thermal power plant. Equally, there are widely differing views about the cost-effectiveness of the proposal.
- The cost of (thermal) power production in BiH suggests that effective value for money considerations would derail the project. This may help explain why the final tender decision is outstanding for over two years.

In 2014, Bosnia's Federation selected a consortium of China's *Gezhouba Group Company Limited* and *Gunagdong Electric Power Design Institute* as the preferred bidder for the

construction of Unit 7 at Tuzla coal-fired power plant. The thermal power plant project is located northeast of Sarajevo in the country's third-largest city.

- Little material progress was made on the project's implementation since 2014. This delay was attributed to the lack of financing arrangements and reservations expressed by European Union institutions concerning environmental requirements and future revenue generation capacity for the power plant.
- In November 2016, the Bosnian power utility *Elektroprivreda BiH* (EPBBiH) signed a framework agreement for the construction of the 450 MW unit at the existing Tuzla thermal power plant (TPP) with China's *Exim Bank*. The deal emerged on the sidelines of the 16+1 summit of the heads of government from central and eastern European (CEE) countries and China in Riga, Latvia.

The framework agreement paves the way towards the finalisation of a loan agreement for the construction project. EPBiH would finance 15 per cent of the project, worth a total of € 722 million. A loan from China's Exim Bank would cover the remaining 85 per cent. Elektroprivreda BiH requested in January 2017 a government guarantee for the loan. The issuance of such a guarantee would be negotiated with the finance and energy ministries of Bosnia's Federation. The Chinese bank is reported to be offering a loan for 20 years with a grace period of 5 years and a repayment period of 15 years.¹⁶ If implemented on these reported terms, the project would be the largest post-war foreign direct investment in BiH.¹⁷

The only large infrastructure project that has been completed with Chinese involvement concerns the *Stanari thermal power plant* in Doboj, Republika Srpska. The project started in 2014 and was completed in 2016. Power production has started. The *China Development Bank* provided a €350 million loan to construct the facility. China's *Dongfang Electric Corporation* was hired by the private owner – *Energy Financing Team* (EFT) – to build the facility. It is thus a private project in RS with no sovereign state guarantee provided.

As regards the EBRD interaction with Chinese representatives, regular meetings with embassy officials are taking place. Chinese companies have started to bid for stretches of motorway projects in which the EBRD is a co-financing partner (e.g. together with the EIB). One such project concerns the *Corridor Vc Motorway*, running North-South in BiH. But so far, no contracts have been awarded to participating Chinese companies. The key reason has been that they were not the cheapest bidders.

These developments on the ground lead us to the following conclusions:

- At the level of the State of BiH there appears to be no strategic roadmap vis-à-vis the question on how to deal with Chinese activities or project proposals. Rather, a case-by-case approach seems to prevail.

- If and where Chinese companies are active in BiH, the reality on the ground in terms of projects that have been agreed, are fully financed and work has commenced stand in stark contrast with the ambitious, but frequently unrealistic intentions of local authorities and political representatives.
- In one specific project in RS, the Chinese involvement in the Stanari thermal power plant underlines that the Chinese are so far only prepared to take construction and limited financial risks, but are not willing to simultaneously take on operation risk.
- Chinese companies are starting to engage in open international tenders based on EBRD procurement rules. But compared to EBRD-Sino project cooperation in Serbia, this development has not yet led to contract awards in BiH. However, it may be only a matter of time until the first EBRD contract will be offered to a bidder from China.

The *Foreign Trade Chamber of B&H* is one of eight members of the *Western Balkans Chamber Investment Forum* (WB CIF), established in Vienna in August 2015. It sees itself as supporting the *Berlin Process* and facilitating any prospective investment by foreign entities. Their contacts with Chinese representatives have been limited so far. The 2017 *Sarajevo Business Forum* (May 22-24) is dedicated to ‘One Economy – One Region’. The rhetorical similarity with China’s One Belt – One Road cannot be mistaken.

The Chinese diplomatic and business-related presence in international conferences is growing. It serves primarily to establish networking opportunities. An increasing importance is being attached to initiatives such as the *Jahorina Economic Forum*, a mountain retreat conference termed the “Davos of BiH”. The Chinese Embassy in Sarajevo is said to have as many staff as the Russian diplomatic representation. However, observers and analysts on the ground report that so far China has refrained from any political involvement in BiH.

Sarajevo is also the seat of the *Regional Cooperation Council* (RCC), established in February 2008 as the successor to the *Stability Pact for South Eastern Europe*. The RCC’s mandate is focused on “developing and maintaining a climate of dialogue, tolerance and openness towards cooperation throughout the SEE region...promoting the European and Euro-Atlantic aspirations of its participants.”¹⁸

To date this mandate does not include any formal contacts or institutional cooperation with Chinese authorities. Neither have Chinese ministries, companies or banks ever contacted the RCC. China does not feature on the radar of the RCC and membership in the RCC is not an option, nor is it feasible (the Russian authorities sought membership in the RCC, but were told that this would not be accepted).

The RCC considers any Chinese requests for cooperation as entirely a government-related matter. Put otherwise, if governments in the region seek these contacts, then it is their decision only. The RCC is not a party to these contacts, nor does it want to become one.

While direct cooperation with, or research activities about, Chinese activities in the region are not on the RCC's radar, it can nevertheless be argued that the RCC is seeking to facilitate regional cooperation in policy areas that can also indirectly benefit foreign investors and/or lenders such as from China. To illustrate, key pillars of the RCC's current 2017-2019 mandate are: (i) connectivity, (ii) mobility, and (iii) providing e-procurement assistance to governments in the region.

In particular the latter activity is of significance for any foreign investor in the region seeking to participate in public tenders today or in the future. The RCC promotes the development of e-services in public administration, working with governments in the region to increase transparency in areas relevant for doing business (e-customs, e-procurement, one-stop-shops for mobility and migration, municipal e-permitting systems). All these types of e-services will become ever more relevant for governments in the region, the more foreign investors, including from China, participate in public tenders and/or provide funding for infrastructure projects along with the arrival of Chinese workers on such projects.

In general, the Chinese activities to date in BiH are limited, signifying more rhetoric than substance. Policy makers and analysts in Sarajevo argue that China is only at the beginning of a much larger engagement in the region of south-eastern Europe. However, doubts remain about the extent to which this will benefit BiH. The political instability of the Federation, unresolved constitutional challenges and geographical reasons¹⁹ are seen as drawbacks that limit an expansion of Sino-Bosnian economic cooperation.

4. Identifying spill-over effects of the BRI

China's engagement in south-eastern Europe is multi-layered. The region can be seen as a testing ground for China's growing European ambitions, whether through the construction of roads, investments in ports, power grids or railways. As China implements its BRI along the Balkan Silk Road spill-over implications materialize over time in particular in terms of regional trade, links to China's manufacturing sector and its commodity exporters.

At this early stage of development, the identification of tangible spill-over effects from the BRI in south-eastern Europe remains a challenging matter. There is no simple or straightforward conclusion about mutually beneficial spill-over effects. China and the 16+1 countries are starting to emerge as partners with common and distinct interests. To complicate the matter of spill-over effects further, their manifestation in macro-economic data is time-sensitive.

With the exception of Greece and to a certain degree Serbia, where spill-over effects are feasible and sustainable over time, the current discussion of positive repercussions for countries along the Balkan Silk Road rather focuses on *soft power* spill-over effects. Put otherwise, the growing Sino-Balkan relationship has diverse implications for individual countries, depending on size of the domestic market, demographics, geographical conditions (e.g. port accessibility or land-locked), level of political stability and progress made in the EU accession process.

While the potential for such spill-over effects from ambitious new (and well established) trade, transport and investment links exists, current developments on the ground in Serbia, Bosnia and Herzegovina and FYR Macedonia suggest that they often seem to fall short when it comes to measurable results. The multiplier effect of major infrastructure investments only manifests itself over time. Individual domestic companies in the construction sector benefit from motorway projects for the duration of such projects. But the sustainability over time remains limited.

The commercial success of the port of Piraeus in Greece following Chinese investments almost a decade ago is an outlier in that respect. The expansion of the port in terms of building additional piers and increasing the volume of container traffic has created sustainable spill-over effects (see section below on anchor investments). But in other countries most local workers on Chinese infrastructure projects represent low-skilled jobs such as trench-digging or lorry driving.

But the overall impact of Chinese investments on GDP growth in the region appears difficult to quantify at present. Few of China's immediate beneficiaries along the Balkan Silk Road can currently claim that Chinese infrastructure investment and closer trade ties have created significant spill-over effects in areas such as SME development, additional job creation or a reversal of existing trade imbalances.

Chinese companies are aware that critics point to these deficits. But they are only at the beginning of pro-actively engaging with civil society representatives, non-governmental organisations, chambers of commerce and universities on issues ranging from the transfer of professional skills, environmental impact assessment or strategic SME development.

All parties concerned agree on the need for a clearer medium-term understanding of the commercial terms of engagement by Chinese companies and political authorities in Beijing. Commerce counts for much – especially when a market the size of China is involved for countries along the Balkan Silk Road whose need for improved export capacity is obvious, but difficult to access new markets.



Source: Compilation based on data provided by *European Council on Foreign Relations*, ‘China’s Investment in Influence: The Future of the 16+1 Cooperation’, ecfr.eu, December 2016, p. 7.

The major contribution of China’s BRI activities in the region of south-eastern Europe is the facilitation of closer trade links and lending activities. Seen from the perspective of Chinese investors and political authorities along the Balkan Silk Road, lending opportunities at preferential rates, infrastructure innovation or increased trading opportunities are judged as a ‘win-win cooperation’.

The most visible spill-over effect in macro-economic terms concerns trade relations within the 16+1 framework. Compared to 2009 levels, total trade between China and countries from central, eastern and southeast Europe almost doubled (see table above). The aggregate data suggests that the volume of exports from CEE countries to China increased by more than 120 per cent during that period.

The marked increase in overall trade volumes could be read as a ‘success story’ for all concerned. But such a conclusion is premature. The increase in trade between China and CEE countries is highly concentrated on five states participating in the 16+1 framework, i.e. Poland,

the Czech Republic, Hungary, Slovakia and Romania who constitute 80 per cent of these trade exchanges.²⁰

Therefore, while trade between China and countries in the Balkans is increasing, the spill-over implications of improved trade relations have a long way to go until they can approximate levels attained in neighbouring countries such as Poland, Hungary or the Czech Republic. One could further argue that with the exception of Serbia, the critical mass of domestic market size and its growth potential just does not exist in countries such as FYR Macedonia, Bosnia and Herzegovina or Montenegro and Albania.

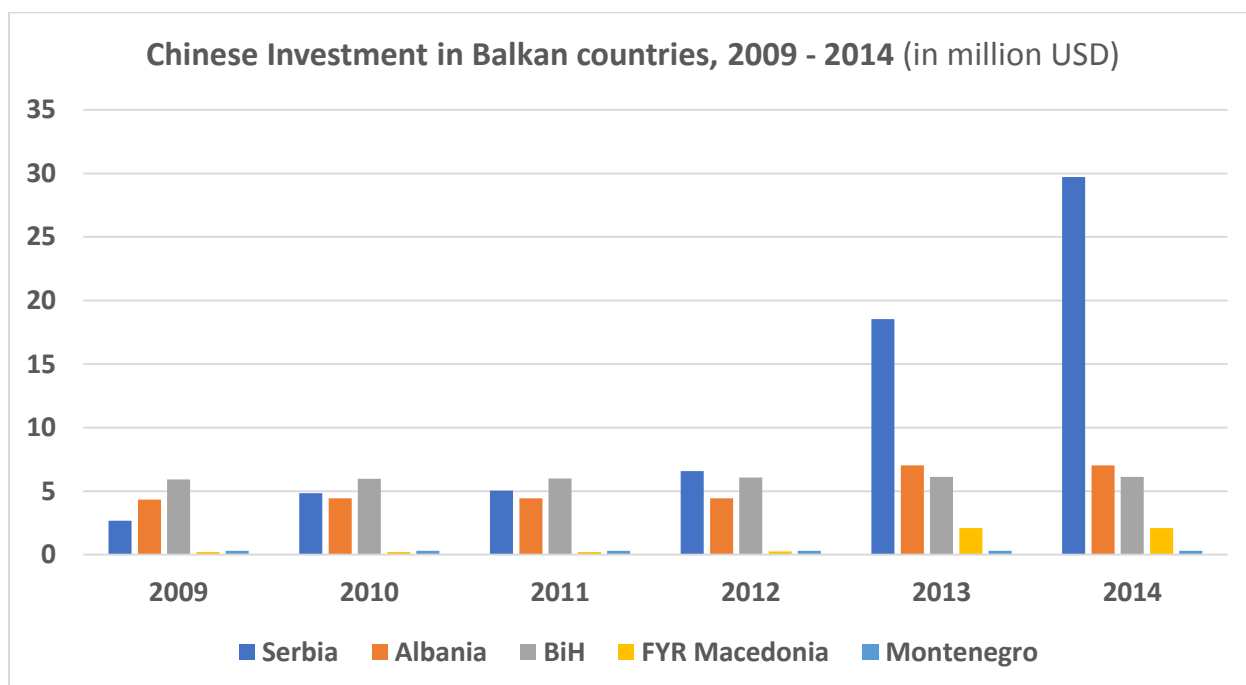
Thus, trade-related spill-over effects in these countries can be expected to remain limited and their increase will rather depend on pooling resources between countries in order to attain critical mass. Furthermore, China's emerging focus on this set of countries must rather be seen as preparing the infrastructure network in order to utilize them as transit hubs or transit networks to move Chinese goods, services and personnel.

The realisation of Chinese-financed transport infrastructure projects will have positive spill-over effects on cross-border trade capacity. Investment in ports, roads, airports and their connectivity should reduce the cost and duration of transportation, thereby potentially contributing to higher trade volumes between China and Balkan economies. Landlocked countries such as Serbia, FYR Macedonia and Bosnia and Herzegovina should also benefit in terms of cross-border regional trade from the reduction in transportation time and costs. A further medium-term spill-over effect could be the establishment of free trade agreements (FTA) between China and the 16 countries in CEE as well as the conclusion of bilateral visa liberalisation regimes.

However, a note of caution on the countries' rising trade exposure with China is warranted. At the macro-economic level the spill-over implications of increased trade with China is based on the assumption that China does *not* become a source of shocks. But as Blagrove and Vesperoni (2016) have observed, "China's economic transition involves rebalancing, which implies that spillovers to different countries depend on their exposure to different sectors of the Chinese economy—secondary sector (predominantly investment) against tertiary sector (more related to consumption)".²¹

The aforementioned geographical trade imbalance is replicated when considering China's outward foreign direct investment in the 16 CEE countries. According to data from the *European Council on Foreign Affairs* (see endnote 19), FDI inflows from China were concentrated in Bulgaria, the Czech Republic, Hungary, Poland, Romania and Slovakia. These six countries took 95 per cent of total Chinese FDI in CEE in 2014.

By contrast, Chinese FDI in individual Balkan economies remains limited and is dominated by an increasing focus on Serbia. However, it should be noted that the available data until end-2014 somewhat distorts Chinese FDI developments in 2015 and 2016. Chinese deal making and investment agreements with countries in the region have markedly increased since end-2014, but are not yet reflected in the available data.



Source: Compilation based on data provided by *European Council on Foreign Relations*, ‘China’s Investment in Influence: The Future of the 16+1 Cooperation’, ecfr.eu, December 2016, p. 9. As Kosovo is not part of the 16 + 1 cooperation framework, there is no official data available regarding Chinese investment in Kosovo, see <http://www.balkan.eu.com/kosovo-left-chinese-investments/>.

Serbia’s geographical and commercial proximity to Hungary can explain its rising status as an ‘outlier country’. Serbia not only constitutes an important market in its own right for China. Investment spill-over effects from Hungary to Serbia and vice versa are possible, illustrated by the high-profile Belgrade – Budapest railway project initiative.

4.1. Anchor investments creating spill-over effects:

The individual investment, lending and acquisition initiatives of Chinese companies along the Balkan Silk Road require over time some form of formalisation and strategic outlook. The two countries where such an approach is most advanced concerns Sino-Greek and Chinese-Serbian economic relations.

In both cases the cooperation between Beijing on the one side and Athens or Belgrade on the other is leading to extensive longer-term economic cooperation agreements that have either been concluded or are at an advanced stage of negotiation. These bilateral pacts include not only a number of specific investment initiatives. They also provide financing mechanisms in terms of lending opportunities, visa liberalisation and cultural exchange programmes.

Such agreements are multi-year deals ranging from three years as a minimum to periods without time limits. Such medium- to long-term horizons provide planning predictability for all parties included. From the perspective of Greece and Serbia the identification of funding mechanisms is most critical, as both countries have limited to no access to international capital markets, and the availability of IFI financing is sometimes regarded as time consuming as well as administratively arduous.

From such cooperation, the participants identify emerging institutional and infrastructure spill over effects. They point to regional and/or bilateral cooperation objectives. The longer and deeper such cooperation takes place with local partners, the higher the capacity for the development of positive feedback loops.

The most obvious of these infrastructure cooperation projects financed by Chinese investment and lending concerns the construction of a fast rail link between Belgrade and Budapest. For both cities, such a project has been on the agenda for more than a decade. Until recently, it did not take off, primarily for lack of financing capacity. In November 2016, China's Export-Import Bank agreed to fund 85 per cent of the bilateral project.

- However, there are two key questions left unanswered in this flagship project. One concerns logistics. The purpose of a high-speed railway line is to transport passengers and cargo. There are serious doubts about the feasibility of cargo travelling at speeds of 200 KM per hour. Moreover, a transparent cost-benefit analysis of the project has been found wanting. International observers on the ground argue that it would be more feasible and cost effective if the existing railway line is substantially upgraded for both passenger and cargo traffic.
- The second issue concerns an investigation launched in January 2017 by the European Commission into the landmark 350 KM railway project against Hungary. The probe is looking into the financial viability of the USD 2.89 billion project. It contends that Hungary is in breach of EU laws by not initiating a proper public tender for a transport infrastructure project of such a financial magnitude.

Such a rail link – if it is implemented – would be part and parcel of a logistics network originating in Piraeus, Greece with onward connectivity via rail links and highways through neighbouring countries and cities. For that reason, Chinese investment is also financing the construction of some sections of Corridor 11, the highway stretching from Romania to Montenegro and then via the Adriatic to Italy.

Developing a logistics network across multiple countries requires an anchor investment from which spill over effects emerge over time. The concept of the anchor investor focuses on companies and/or state authorities seeking a reassuring buttress over the medium to long-term. The initial Chinese company COSCO investing since 2009 in the Port of Piraeus is such an

anchor investor which generates various follow-up activities in terms of lending, acquisitions and diversification into other sectors.

Piraeus will enter the list of the world's 30 biggest container handling ports in 2018. The launch of West Terminal III is expected to lead to a huge rise in annual capacity. Piraeus Port Authority head Fu Cheng Qiu expects the Greek port to handle around 5 million containers in 2018. Such capacity expansion is in line with the objective to turn the port into a transshipment hub between Asia and Europe.

To illustrate: In 2016 container handling in the Greek port of Piraeus, the largest commercial port *COSCO* operates outside China, recorded an all-time high of 3.47 million units. This represented an increase by 14.4 per cent on 2015 figures. In the period from 2007 to 2016 container handling grew by a total of 167.7 per cent. In terms of container traffic perspectives, there seems to be no limit in sight. In the first four months of 2017 container handling traffic rose 5.2 per cent year-on-year.

Anchor investments can serve as catalysts, thereby attracting additional companies and expansion into other sectors. The Sino-Hellenic cooperation highlights such spill-over effects prominently. The Greek telecoms company *Forthnet* and the Chinese telecom equipment maker *ZTE Corp.* teamed up in April 2017 with two other Chinese firms to finance the construction of a fiber-optic network in Greece.

Equally, the Greek case can also illustrate how an anchor investment in one country serves as part of a larger emerging puzzle of a stated strategy. Put otherwise, Chinese anchor investments can be catalysts for additional equity funding in the same sector in other countries. Consequently, a cross-border cluster of investments is established whose expansion gradually creates a regional assets portfolio.

To illustrate, in June 2017 *COSCO Shipping Ports* agreed to purchase a majority stake in *Noatum Port Holdings*, the operator of container ports in Valencia and Bilbao, for €203 million. Apart from the acquisition of additional container terminals in two Spanish port cities, COSCO also received rail terminals in Madrid and Zaragoza. Such investments form integral parts of a multi-decade and multi-country strategy.

In the words of COSCO, the stated objective is to “develop[-e] a global terminals portfolio”.²² This would put the state-owned shipping company in a position to challenge European rivals such as *Maersk* or *Mediterranean Shipping Company* on their home continent. Such Chinese investments seek to control strategic assets. The ownership of ports from Australia to Greece, and Albania to Spain expands infrastructure assets while broadening the capacity for trade links with Asia and Europe.²³

In the case of FYR Macedonia, the construction of the A2/A3 highway from Kicevo to Ohrid and the Miladinovci to Stip motorway constitute two Sino-FYR Macedonian infrastructure projects. They have created multi-year construction jobs for two domestic companies working as sub-contractors. When completed in the second half of 2017, both motorways will be able to

alter transport logistics in the country. But they can also serve as a magnet for future business and investment activities. Both motorways facilitate and reduce travel time along an East-West corridor, improving connectivity from the capital Skopje to eastern and western regions of the country, including to adjacent border crossings.

Tangible multiplier effects on job creation and growth for SMEs along the Balkan Silk Road can be expected to emerge over time. The potential for such benefits to take root will only increase if and when Chinese companies seek to involve a larger degree of local expertise and domestic firms, instead of providing (major) parts of the workforce and planning personnel from China proper. Making such a domestic approach a policy requirement when Chinese companies compete for public tenders – in particular for EBRD- and EU-related tenders - should be considered as a conditionality during the bidding process.

But the advocacy of spill-over effects must be placed in context. Is value for money apparent? What return on investment is feasible? The potential benefits of a new high-speed railway line between Budapest and Belgrade may be obvious for passenger traffic, but less so for commercial traffic. In other projects such as the modernization of coal mines into thermal-power plants (e.g. state-run coal mine operator Banovici in Bosnia and Herzegovina), the potential job creation effects during the conversion process must be measured against the anticipated costs of producing thermal power and its sale price on domestic as well as international markets.

4.2. Secondary spill-over effects:

There are also other spill-over effects that materialize over time in a variety of sectors. Some of these secondary spill-over implications respond to immediate cooperation needs that arise, while others are the result of regulatory requirements. To illustrate:

- **Bilateral and cross-regional cooperation among economic councils and chambers of commerce** have become a matter of urgency as a result of the Chinese investment drive.
 - The *Greek-Chinese Economic Council* was established in 2013. The council plays a coordinating role in the collection, processing and promotion of investment proposals, drawing up business plans for a variety of sectors.
 - The *Chamber of Commerce and Industry of Serbia* is establishing a Centre for Relations with China and it is a member of the 16+1 (16 chambers of commerce plus China).
 - The *Western Balkans Chamber Investment Forum* (WB CIF) was established in Vienna in August 2015. The creation was a joint initiative of the *Chamber of Commerce and Industry in Serbia* and the *Kosovo Chamber of Commerce*. Its primary objective is the implementation of policy initiatives resulting from the *Berlin Process*. The WB CIF has eight members from the region, i.e. from

Albania, Bosnia and Herzegovina, Montenegro, Kosovo, Croatia, Macedonia, Serbia as well as Slovenia.

- It is noteworthy that while Kosovo is not included in the 16+1 format, it is a founding member of the WB CIF. In that respect, the joint initiative with the Chamber of Commerce and Industry in Serbia can be regarded as being a step ahead of politics in Belgrade concerning the non-recognition of Kosovo.
- This Forum offers a platform for policy coordination, identifying synergies and streamlining regulatory issues with prospective foreign investors, including from China. First attempts towards joint action can already be identified in the area of cultural tourism, software engineering, and food exhibitions.
- A key factor facilitating economic and commercial ties along the Balkan Silk Road will be **visa liberalisation**. In this area, the role of embassies and consulates is critical. Foreign ministries from Greece, Serbia, Hungary and FYR Macedonia are accelerating visa-issuing procedures at the respective diplomatic representations in Beijing.
- Chinese infrastructure investments in highways, bridges and power plant modernisation are also viewed as laying the groundwork - in an optimistic scenario – for the development or expansion of local **SMEs**.
 - On closer inspection, this assumption needs to be qualified. For the most part, Chinese investment and/or lending in Serbia, Bosnia and Hercegovina and FYR Macedonia features Chinese financial resources, workers and strategic planning.
 - Greece is an outlier in this respect. Chinese investment is not only more advanced in terms of duration and diversity of sectors. It is also based on Greek companies in which the Chinese are the majority owners, but agree to employ the local work force.
- Chinese economic cooperation within the 16+1 framework can also be related to current and future privatisation opportunities as well as participation in forthcoming public tenders for large-scale infrastructure projects. The success of two Chinese companies being awarded EBRD contracts in Serbia can be seen as gradually ‘learning the ropes’ of public procurement opportunities with such multilateral lenders. It is a matter of time until this experience spills over to other countries, EBRD offices and EU delegations in the region.
- Another example of spill over effects concerns initiatives to create **Chinese-speaking** [higher] education centres in countries participating in the Balkan Silk Road. To illustrate, in Athens and in Belgrade, Chinese embassies are interacting with local public and private schools to increase the availability of learning the Chinese language.
- The objective to strengthen the **cultural interaction** between countries along the Balkan Silk Road is a recent initiative fostered by the Directorate General for Education and

Culture of the European Commission in Brussels. In a statement the DG head, Martine Reicherts, argues that “the ancient Silk Road stood for more than just commerce. For centuries, it enabled people to move, cultures to blend, and knowledge to be exchanged.”

- To illustrate this increased awareness, the China-Greece *Cultural Exchanges and Cultural Industry Cooperation Year* was launched in Athens in April 2017. On the occasion two memoranda of understanding were signed on film co-production and translation and the publishing of classic and modern Greek and Chinese literary works.

5. Identifying barriers

This chapter will focus on the identification of key barriers to unlocking the growth potential in the CSEE region brought by BRI investments, infrastructure projects and logistics developments. It cannot come as a surprise that such a massive and long-term FDI strategy has its critics and faces numerous obstacles on its way to implementation.

The former chief economist of the World Bank, Lawrence Summers²⁴ termed China's approach "authoritarian mercantilism", underlining the central role of state institutions and a host of its enterprises promoting access to global markets through the vehicle of foreign investment expansion.

As Chinese-led BRI investments progress in EU as well as non-EU countries, current or future barriers arise. These barriers can be the result of a lack of communication to affected parties about the rationale of Chinese investments, their growth potential and long-term objectives. Such barriers can be established by different constituencies, who may call for domestic and/or European regulation, if not intervention. To illustrate:

- There is a growing concern about rising trade imbalances between China and countries along the Balkan Silk Road. To illustrate: during the first six months of 2016, Serbia imported US\$ 773 million worth of goods from China, while only exporting US\$ 12 million.
- Trade unions, employers' associations, civil society organisations or even regulatory authorities in countries along the Balkan Silk Road Initiative have called for the increased monitoring of Chinese investments that risk creating trade imbalances and potential dependency on loans and credits.
- Such calls address the need to define what constitutes relevant (technological) sectors that are deemed to be "protected" from foreign takeovers. This debate is taking place in Germany, Greece and gradually gaining currency in countries of south-eastern Europe.
- This 'protectionist' debate includes the recurring issue of industrial or manufacturing clusters, and how they can be enlarged, financed and regulated vis-à-vis increasing Chinese investment interest.
- The flip side of this controversy concerns erecting potential barriers for Chinese firms in European destination countries while at the same time governments and businesses are calling on the Chinese authorities to lower investment barriers for foreign investors in China.
- A key financial barrier consists in the allegation that Chinese acquisitions and investments are state-funded subsidies that undercut competitors in selected sectors. The EU Delegations in Serbia, Bosnia and Herzegovina and in FYR Macedonia are aware of

this policy conundrum, in particular when concessional lending by Chinese state-owned banks does not include a public tender process.

- Furthermore, a frequent criticism heard in Belgrade, Skopje and Sarajevo focuses on the view that countries in the region receive so little FDI from Europe that China becomes by default the only country to turn to.
- There is a certain disconnect between the list of prospective investments by China in individual countries and the reality of agreed finance, matured projects and commenced work on the ground. This raises the question of substance versus rhetoric, the political instrumentalisation of Chinese activities and the lack of coherent communications policies.

These institutional, policy-related and financial barriers are not insurmountable. A focused policy dialogue with various constituencies, including civil society representatives, in targeted countries can garner support in accessing the potential opportunities and tackle impediments that currently exist.

Chinese investors are very aware of how they want to present their initiatives in Europe. In doing so, they can address critical aspects that concern investment and lending decisions, e.g. what are the boundaries between Chinese development aid, influence-buying, profit-oriented investment and projects motivated by resource security concerns? The more BRI-specific activities can create tangible spillover effects in countries along the Balkan Silk Road, e.g. in terms of SME growth, job creation and trade facilitation, the higher the chances that the rationale for Chinese activities is seen as mutually beneficial for all sides concerned.

A comprehensive and rather critical assessment of China's New Silk Road project was recently formulated by *Clingendael*, the Netherlands Institute of International Relations.²⁵ With Beijing underwriting billions of euros of infrastructure investments in the western Balkans and the Black Sea, the authors argue that the potential for transformation in specific sectors is enormous.

However, they also emphasize that China's ambitions will have to reckon with Russia on the one hand, and the European Union on the other concerning the development and economic integration of the region. A further point of contention concerns what officials in Brussels say are aggressive tactics by Beijing to leverage Europe's energy supply to extract diplomatic concessions.

Other critics²⁶ of the Chinese investment drive along the Balkan Silk Road argue that the surge of (concessionary) lending to individual countries in the region – which can amount to a large percentage of a state's gross domestic product (e.g. in Montenegro) – raises concerns about China's leverage over such countries, e.g., when a state falls behind on debt repayments. The repayment capacity of government institutions or domestic firms subject to Chinese loan agreements is not obvious. The danger of loans not being repaid in full and on time may open the door for subsequent political influence by Chinese counterparties. However, it must be underlined that to date no such cases have come to light.

A major barrier to implementing China's globalization blueprint in European countries became apparent at the recent high-profile "*Belt and Road Forum*" in Beijing (May 14-15, 2017). Various EU member states declined to sign the proposed trade statement which Beijing had drafted. Key objections were voiced concerning the lack of transparency references, together with open, rules-based public tenders and reciprocal market access. The European attention to fair and transparent procurement practices is a reflection of concerns that Chinese companies are to benefit in future Silk Road contracts, while sidestepping standards in tendering contracts.

6. Recommendations for the EBRD

This concluding chapter seeks to provide policy recommendations to the EBRD project team. The recommendations focus on how best to support the region in maximizing the growth potential brought by BRI investments. China's BRI overlaps with about half of the EBRD's countries of operation. Hence, the potential scope of Sino – EBRD cooperation is considerable. But such cooperation would also come under increasing scrutiny, e.g. regarding compliance requirements.

Since January 2016 China is a shareholder in the EBRD and its 67th member. Gradually, a Sino – EBRD project relationship is emerging. It includes public tenders being awarded to Chinese companies in Serbia and loan securitization in FYR Macedonia. Furthermore, in June 2016 a cooperation agreement was signed between the EBRD and the *Silk Road Fund*. China also became a cornerstone investor in the *Equity Participation Fund* (EPF) launched by the EBRD in September 2016. The *State Administration of Foreign Exchange* (SAFE), a sovereign wealth fund from China, committed €250 million to the EPF.

The evolving Sino-southeast Europe relationship is not monolithic. The engagement includes multiple players with different, at times conflicting agendas. The 16+1 cooperation format enables countries in central, eastern and southeast Europe to conduct business with various Chinese lending institutions, state-owned enterprises, central and regional governments, private companies and diplomatic representations.

The expanding activities of China in Greece, Serbia, FYR Macedonia, Albania, Montenegro, Bosnia and Herzegovina and Hungary pose challenges for EU Delegations, Commission Representations and multilateral lenders such as the World Bank, the European Investment Bank and the EBRD. They must decide how to set priorities and negotiating with Chinese companies that are seeking to make acquisitions or participating in public procurement tenders.

As the EBRD has recently developed a new *Transition Concept*, the application of its key elements faces challenges and opportunities as regards the Chinese surge of activities in the Balkans and Black Sea region.²⁷ It can be regarded as a formidable medium-term test case for the validity of this new concept and how it can be made operational in the interactions with Chinese investors and lenders seeking access to countries of operation of the EBRD.

To illustrate, the quality of “well-governed” addresses governance issues such as procurement rules, the pricing of loans and the impact on local economies that need to be addressed with Chinese counterparties active in Serbia, Bosnia and Herzegovina, Albania or even Greece. Like any other cooperating project partner of the EBRD, e.g., in public tenders, Chinese companies will be evaluated on the basis of how their activities facilitate the sustainability of market reforms.

Overall, Chinese investments along the Balkan Silk Road are welcome by policy makers in the region. This willingness is based on a pragmatic approach on behalf of countries in the western Balkans. They remain committed to the twin objectives of European Union accession and NATO

membership. Despite visible inroads being made by Chinese companies, the main economic anchor remains with Europe.

This anchor is by far still the region's largest source of investment and development assistance. Therefore, it is more appropriate to consider China as a complement to, rather than a substitute for, the Balkan countries' European partners. China is an additional source of funding and infrastructure modernization. But it is not yet a replacement for any of the countries in the region. At a time when investments in Greece are considered too risky by most foreign counterparts, Greece has found itself a potential ally in China.

However, existing multilateral IFIs such as the EBRD need to recalibrate their approaches to compete more effectively in an increasingly Sino-centric region along the Balkan Silk Road. For its part, China can only gain from embracing transparent governance standards in lending arrangements with countries participating in the Balkan Silk Road. This forms part of building reputational capital to match their existing funding capacity.

6.1 Fostering policy dialogue

The magnitude and complexity of the Balkan Silk Road project poses numerous policy challenges for countries in the region engaging in or seeking to benefit from its implementation. As highlighted in the previous section, these challenges are substantial, ranging from a critical assessment of the project's objectives, the process of stakeholder inclusion, regulatory capacity-building and co-financing requirements.

Such policy challenges cannot be solved by individual countries single-handedly. They require advisory services and institutional guidance from international organizations familiar with the host country and capable of interpreting the challenges and opportunities of the Chinese initiatives. It is at this critical intersection that an international institution like the EBRD, active in 36 countries that stretch from central Europe to Central Asia and the southern and eastern Mediterranean, has a key role of interlocutor to play.

On a macro level, two aspects deserve greater inquiry. It is not always clear from China's potential partners in the Balkans and the Black Sea region what they in fact expect from participation in the BRI. These countries' co-financing capacities are limited. Equally, many of the infrastructure projects can improve economic productivity in the medium term. But it remains an open question, to what degree certain transport links can be monetized. Ports and pipelines appear easier than thermal power plants and road infrastructure.

This raises the question, who bears short-to-medium-term losses regarding financing, revenue streams and maintenance costs? If many of these projects are designed primarily to transport and distribute Chinese goods to different locations in Europe, then the one-way traffic along new trade routes will hardly be cost effective. These emerging international supply chains would undoubtedly benefit more if they are operated on the basis of two-way traffic.²⁸

It should further be borne in mind that the emergence of a China-led financial architecture of new multi-lateral banking institutions requires an organisation like the EBRD to identify its strategic relationship with these. Put otherwise, how can the EBRD try to maximize its role alongside China in the new financial architecture? In short, the EBRD must decide whether to become a stakeholder in a grand project currently being defined primarily by China.

This implies e.g. identifying synergies between the EBRD and Chinese financial institutions as regards the growing demand for financial and technical assistance in infrastructure investment in south-eastern Europe. The EBRD has gained valuable policy expertise in this area during the past three decades in the region, while China has accumulated enough foreign reserves to contribute to such endeavours.

Mixing and sharing this know-how of the EBRD with the financial resources and investment determination of Chinese companies can be a ‘win-win’ combination for both parties. Countries in south-eastern Europe see in China the opportunity to provide them with the financial assistance to build highways, expand harbours and modernize utility facilities. But they equally require the presence of institutional anchors such as the EBRD, the EU delegations, the IMF and others to navigate the procurement process, and safeguard financial transparency and regulatory fair play.

The engagement of the EBRD in policy dialogue and the provision of technical advice are crucial in such a multi-layered, long-term investment project as the Balkan Silk Road. In order to generate support within governments and civil society in the Western Balkans and the southern and eastern Mediterranean, it is proposed that the EBRD should focus on five fields of engagement.

These five fields are identified for two reasons. Firstly, on the basis of a needs assessment resulting from interviews (by the consultant) with stakeholders in various countries along the Balkan Silk Road project. Secondly, the EBRD has developed numerous advisory and financing arrangements in its countries of operation that can provide policy makers with a toolkit of existing instruments without having to ‘reinvent the wheel’ wholesale. Rather, the EBRD should use current and tested instruments while fine-tuning them where necessary to the specifics of the Balkan Silk Road projects.

1. Ministries, regulatory agencies and municipalities subject to investment initiatives within the framework of the Balkan Silk Road projects are frequently overstretched with regard to the licensing requirements, financial implications, zoning regulations and European Union legal obligations (e.g. granting of subsidies) that encompass cooperation with Chinese counterparties.
2. The crucial element for governments in the Balkans is how to take control of their relationship with Chinese counterparties? The local presence of the EBRD in these

countries can provide valuable additionality in the context of advancing complex policy dialogue, setting policy priorities and establishing negotiating skills on their own terms.

- a. To illustrate: For the Serbian authorities, the process of including all ratified (Chinese) project loans in the budgetary reporting process on a yearly basis has yet to be fully understood. Contributing to such a level of transparency should form part of the policy dialogue and monitoring process of the EBRD vis-à-vis the Ministry of Finance and the Central Bank. The IMF representation in Belgrade has repeatedly addressed this requirement to its Serbian counterparties.
 - b. A second area of strategic policy dialogue concerns the lending practices of Chinese banks. Concessional loans offered to Serbian counterparties reduce or even abolish the need for co-financing. This business practice affects EBRD lending policies, including the subsequent tendering process with local authorities, pricing levels and transparency requirements.
 - c. In the Serbian case the prevailing contract arrangement has been EPC contracting plus credit lines from Chinese banks (e.g. the flagship railway reconstruction project Belgrade – Budapest).
 - d. However, countries involved in EPC contracting with Chinese authorities require guidance on how to record the impact of EPCs on government accounts. The key challenge is how to determine the allocation of capital expenditure (gross fixed capital formation in national accounts), related to specific assets which take place in different phases of the contract. The EBRD, EU Delegations and IMF representatives in host countries need to draw closer attention to these implications vis-à-vis finance ministries and central banks.
3. As a multilateral development bank, the EBRD can bring innovative financing and technical assistance to economically viable projects along the Balkan Silk Road project route. The financing arrangements at the disposal of the EBRD (e.g. PPPs, guarantees, loans and equity) should be linked with products and programmes from other IFIs in order to reduce countries' reliance on Chinese financing resources.
 - a. To illustrate: The EBRD office in Belgrade awarded two tenders to Chinese companies in 2016. This experience provides opportunities to build and expand a relationship between both sides, starting with adherence to EBRD and/or EU procurement rules and thereby establishing a track record of credibility that Chinese companies still require. Fostering such contract relationships could prove an invaluable EBRD contribution in the medium-term.
 - b. Another area of harnessing policy dialogue concerns the current focus of many Chinese investments and/or lending agreements in the energy sector in south-eastern Europe. In cooperation with institutions such as the EU Delegations, the Regional Cooperation Council and the respective line ministries the EBRD

should emphasise that e.g. thermal power plant construction requires stringent compliance with environmental standards and an environmental impact assessment.

- c. As the Balkans and the Black Sea regions appear to become key Chinese entry points for trade and investment exchanges with Europe, the EBRD should consider expanding its networking capacity with the *Organisation of the Black Sea Economic Cooperation* (BSEC), the *Black Sea Trade and Development Bank* (BSTDB) and the *European Banking Federation* (EBF) as strategic partners.
4. As the Balkan Silk Road project is first and foremost about trade expansion, the EBRD's *Trade Facilitation Programme* (TFP) should make full use its opportunities in the countries of operation. This could include EBRD guarantees to commercial banks concerning payment risk of trade transactions.
 - a. To illustrate: Selected domestic commercial banks receive a pre-approved credit limit to support the export, import and local distribution of imported goods and services. The EBRD's TFP would focus on assisting domestic lenders to scale up their trade finance activities.
 - b. The existing 16+1 format focuses on investments and the willingness of countries in central, eastern and south-eastern Europe to expand trade cooperation with China. The surge of Chinese exports to most of these countries has further increased the trade deficit with China, in particular in Poland, Romania and Hungary.
 - c. The EBRD should consider to what degree it can advise participating countries in the 16+1 format concerning their bilateral trade imbalances with China. Here the interaction with domestic Chambers of Commerce and regional platforms such as the WB CIF may harness better synergies.

5. The existing business model of Chinese companies active in the region is hardly supportive of the local economy. Providing lending and foreign workers bypasses domestic banks as well as local expertise on the ground. In this respect, even concessional lending by Chinese banks, frequently praised for its lower costs, may in fact not be as cheap without spill over effects materializing on the local economy. Equally, concessional lending requires no local content stipulated in the contracts.

Thus, one of the challenges for an institution such as the EBRD, but also for EU Delegations, who both have a network of representative offices in the region, is how to garner more value added from Chinese companies.

The EBRD's existing *Small Business Initiative* (SBI) is in a position to provide small and medium-sized companies with advisory services and complementary financing options when these engage in projects linked to the Balkan Silk Road. But it can also

attempt to nudge Chinese contractors having been awarded an EBRD tender to engage more pro-actively in supporting local economic structures and facilities.

- a. To illustrate: The more infrastructure projects along the Balkan Silk Road take root, the more people and businesses have opportunities to be connected. This will take time and does not immediately benefit SME development in individual countries. But a proposed road project such as the Novi Sad – Irig – Ruma linking Serbia with Croatia and Bosnia and Hercegovina comprises more than 370,000 residents and approximately 30,000 SMEs along the way.
 - b. The Chinese investment in the Serbian steel mill *Zelezara Smederevo* is a commitment to upgrading existing infrastructure and represents opportunities for technological transfer. Such investments, less so lending, are entry points for SME development because the new Chinese owners will also have to rely on local workers, logistics networks (water, electricity, roads) and municipal, regional decision makers. Therefore, the EBRD's SBI can assist in the process of building commercial and job-related relationships between Chinese and local Serbian SMEs.
6. The final field of engagement in policy dialogue concerns a critical assessment of the Balkan Silk Road project in terms of establishing investment dependency for countries in the region.
 - a. To illustrate: Medium- to long-term growth perspectives in individual countries subject to the Balkan Silk Road project are at risk of excessive dependence on Chinese state investment, in particular state-owned and/or state-dominated companies.
 - b. Many of these Chinese companies suffer from heavy indebtedness and export overcapacity. If Chinese authorities were to rein in lending practices to these companies, the potential spill over effects to their subsidiaries in the Balkan region could be considerable in terms of curtailing existing investment plans, job creation commitments and SME development outlook.
 - c. Moreover, it is necessary to question the reliance on the top-level design of business practices and investment plans that characterises many Chinese companies involved in the Balkan Silk Road project.²⁹
 - d. In cooperation with EU Delegations, the IMF, World Bank, etc. EBRD offices in the Balkans and the Black Sea region should continuously emphasize the rules of engagement for bilateral trade, transparent financing and open procurement practices. Chinese road building goes hand-in-hand with transparent corporate governance.

Appendix A. China's New Silk Road: The Belt and Road Initiative (BRI)

China's *Belt and Road Initiative*, launched under President Xi Jinping in 2013, is China's most ambitious south-to-south cooperation plan. The aim of BRI is to connect Asia, Europe and Africa across more than 60 participating countries. The channels to achieve this ambitious initiative are through improved and accelerated economic trade across multiple corridors. They seek to mobilize investments in various sectors such as transport, logistics and energy.

Investments and lending originating from Chinese sources has gone to countries as diverse as Russia, Indonesia, Brazil, Argentina, Iran, Egypt, the Philippines, Pakistan, and to a lesser degree to India and Japan.³⁰ The African continent has 13 participating countries so far.³¹ In Europe, China is actively acquiring specialized manufacturing companies, in particular in Germany, Switzerland, the United Kingdom and France.

To date, 56 economic and commercial zones have been established along the BRI. According to a recent report from *Credit Suisse*, the total BRI investment in the next five years is to be in the range of USD 313 billion to 502 billion.³²

However, in 2016 investment from the BRI declined. According to Chinese sources in the Commerce Ministry reported by the *Financial Times*, foreign direct investment from China to countries identified as part of the BRI fell two per cent year-on-year in 2016. It dropped an additional 18 per cent in the first quarter of 2017. Non-financial FDI to BRI countries totalled USD 14.5 billion in 2016, comprising nine per cent of overall outbound FDI.³³

The BRI along with its industrial ambitions and investment outlook underscores a new far-reaching phase in China's aims. These days, Beijing and Shanghai are full of expansion plans in a host of political economy areas. Under a complimentary plan called *Made in China 2015*, China hopes to become largely self-sufficient within eight (!) years in a long-list of industrial sectors.³⁴

These sectors include aircraft, high-speed trains, computer chips and robots. The check book for this self-sufficiency drive is estimated at 300 billion USD in financial resources. It includes inexpensive lending from state-owned banks, investment funds to acquire foreign technologies and extensive research subsidies.

Placed in such an expansionary framework, the BRI is a long-term political economy strategy that represents a fundamental shift in how China seeks to deal with countries on a global scale. The BRI focuses on connectivity and cooperation among countries along two main routes:

- (i) The "Silk Road Economic Belt", aimed at facilitating land-based trade across the Eurasian landmass;
- (ii) The "21st Century Maritime Silk Road", which aims to use Chinese coastal ports to link China with Europe and the South Pacific through oceangoing corridors.

Beijing's strategic initiative has mobilized countries and international organisations across continents like no other Chinese project before. According to various accounts, 65 countries and numerous international organisations have expressed their interest to participate in the New Silk Road. On this scale, BRI is seen by countries and organisations involved as a "geo-economic and geo-political strategy, rather than just a soft power initiative".³⁵

On 14.-15. May 2017 heads of state, prime ministers, representatives from international organisations (UN, IMF, World Bank, EU Commission, etc.) and multinational companies participated in a summit dedicated to the new *Silk Road Initiative* in China's capital. The *Belt and Road Forum* served to highlight China's determination to be recognized on a global stage as a leading protagonist of international economic cooperation.

Hosting this first major summit did not turn out to be the kind of success story the Chinese authorities were expecting to propagate. Only 29 national leaders joined the summit. Important regional powers such as India and Japan did not participate at the level of government leaders in China's signature economic-diplomacy initiative.³⁶ The next BRI summit is scheduled for 2019.

EU Member States, including Germany, France and the United Kingdom declined to sign the summit's closing statement on trade. They expressed reservations about its omission of references to social and environmental sustainability standards as well as transparency requirements in tendering contracts for infrastructure projects as well as their financing architecture.

A grand design such as the BRI requires laying the foundations for a Sino-centric financial architecture. To that end Beijing has made considerable efforts to provide and diversify financial resources. BRI includes special lending schemes in excess of USD 50 billion and a *Silk Road* fund worth USD 40 billion.

Moreover, China is establishing financial institutions that mirror its global development agenda. This includes the creation of the *New Development Bank* (NDB) as well as the *Asia Infrastructure Investment Bank* (AIIB).³⁷ The setting up of the *Development Bank of the Shanghai Co-operation Organisation* complements this new financial architecture. These three institutions add to the financial firepower available to the *China Development Bank* and the *Export-Import Bank of China*.

The BRI reflects China's long-term ambitions and current economic capacity. China is the world's largest manufacturer, biggest exporter and largest domestic market for cars, mobile phones and oil products. China is now home to two-thirds of the world's solar production capacity. When measured by purchasing power, according to the IMF, China became the largest economy in the world in 2014.

China is today the biggest export market for a total of 43 countries (and growing in numbers and volumes). Reflecting this trend, in 2016 China became Germany's largest trading partner. Such a massive shift in trade flows and demand has geopolitical consequences. These are most pronounced for China's trading partners in the Asia-Pacific region, including Japan, Australia,

the Philippines and South Korea. The importance of their economic relationships with China is growing by the day.

The leverage acquired by China through this development and how it is used today and in the future by the political authorities in Beijing occupies policy makers and analysts. The availability of Chinese loans, infrastructure investment and imports of goods while gaining a foothold in a massive export market can contribute to modulating criticism of China's domestic challenges such as human rights record, access for foreign firms and foreign policy priorities.

The investments that China has executed in the region of south-eastern Europe in the course of the past decade form an integral part of BRI. Their strategic logic is apparent from the (initial) focus on transport infrastructure and implementing investments in individual countries with a view to a comprehensive regional approach.

The concern that arises from these activities focus on the follow-up question to what degree governments can afford to ignore Beijing's wishes? China's growing significance as a trading partner and investor for countries in south-eastern Europe has its merits and simultaneous critics.

As a foreign direct investment strategy, the BRI faces domestic hurdles. For one, existing capital controls in China require that the Chinese government needs to approve such FDI initiatives for state-owned, semi-private and fully privatized companies. This approval process is usually positive when the investment or acquisition complies with the strategic rational of the BRI.

The capital controls which were introduced in November 2016 seek to control currency exports. The key interest of the Chinese government is to make sure that cross-border acquisitions do not weaken the domestic currency *Renminbi*. Put otherwise, Beijing wants to prevent a depreciation of its currency as a result of increased foreign currency outflows.

A1.1. The priorities of BRI

For the region of south-eastern Europe, two countries stand out along the *Balkan Silk Road* project, namely Greece and Serbia. The Chinese BRI has five key priorities. They shall be briefly highlighted below.

Policy Coordination

Countries along the BRI routes are to work together to formulate development plans and engage in practical co-operation and large-scale project implementation, as well as resolve any problems that arise from co-operation through consultation. One such potential coordination avenue is the 16+1 format established in 2012 between China and 16 participating countries from central, eastern and south-eastern Europe (see chapter 4).

The 16+1 club includes current and non-EU members, NATO members and EU candidate countries as well as five euro area participants. It is also apparent that within this list a number of

countries are absent. For one, it should be noted that Greece is not a member in the 16+1 arrangement. It has an observer status. Furthermore, neither is Kosovo a member, nor do Turkey and Ukraine participate.

Facilities Connectivity

Enhancing and financing connectivity is a key pillar of China's activities in the region of south-eastern Europe. It is equally a central benchmark of the EU accession process. Furthermore, in specific sectors such as transport infrastructure, future connectivity improvements can yield substantial benefits. According to estimates from the *Regional Cooperation Council* (RCC) in Sarajevo, more than 500 trucks pass from Turkey to Germany through the Balkans on a daily basis.

Prioritisation of new infrastructure, and advancing infrastructure facilities that promote connectivity such as railways, highways, air routes, telecommunications, oil and natural gas pipelines and ports, are also key priorities. This aspect of connectivity is multi-layered, pending on sectors, investment capacity and regulatory oversight.

For EU and non-EU member states, the Chinese investment drive via the Balkan Silk Road Initiative offers the opportunity for international expansion, enlargement of production capacity and the development of new products and services. These opportunities lack the financial resources from host governments and domestic companies. The Chinese investors represent the openings that would otherwise hardly materialize.

The connectivity that a deep-pocketed investor such as China can provide allows for projects to go forward since the financing conditions appear less time-consuming and administratively arduous than seeking these resources on international capital markets and/or through multi-lateral public financing institutions (e.g. IFIs).

There is a further element of connectivity that should not be underestimated. This involves the opportunity for companies and utilities to gain or enlarge their access to European and even global markets that would otherwise not be available. Chinese companies can therefore create strategically relevant access routes for enlarged and diversified trade and export capacity in countries along the Balkan Silk Road Initiative. Put otherwise, with the 'help' of a large sister company in China, doors open for European firms in international trade. The (potentially positive) reputational side effects of this process are key.

China's emphasis in the BRI is to build and connect global champions through industrial policies, investment initiatives and lending opportunities. These activities raise concerns about China's commitment to a mutually beneficial relationship. Among policy makers and observers in Athens, Belgrade, Sarajevo and Skopje there is some realization that the commercial and investment relationships are highly asymmetrical. But there is scant evidence that this concern is being addressed in some way by domestic policy makers. If at all, then it is carefully voiced by

IIFs and multilateral lenders such as the IMF, the EBRD and to a certain extent by central bank representatives.

Unimpeded Trade and Investment

Resolve investment and trade facilitation issues, reduce investment and trade barriers, lower trade and investment costs, as well as to promote regional economic integration.

The strategic investment logic of BRI in Europe can be further illustrated by expanding the focus from Greece and the Balkan Silk Road to included countries such as Germany. The German companies acquired in the course of 2016 by various Chinese firms are primarily located in the manufacturing sector, with a special emphasis on technological innovation.

Chinese Merger & Acquisition Deals in Germany in 2016 - 2017

CHINESE COMPANY	ACQUIRED GERMAN FIRM	PURCHASE PRICE (IN BILLION USD)
MIDEA	Kuka*	4.663
BEIJING ENTERPRISES	EEW	1.594
CHINA THREE GORGES	Wind MW	1.440
CHEMCHINA	KraussMaffei	1.011
IDG, MLS, YIWU	Ledvance	0.400
TECHCENT	Alba (partly)	0.300
GENTING	Nordic Yards	0.250
NINGBO JOYSON	Technisat	0.236
TECHCENT	Bilfinger Water	0.223
LIAONING DARE	Carcoustics	0.200
NINGBO JIFENG	Grammer (2017)	0.060
HNA GROUP	Deutsche Bank (2017)	(9.92 % Shareholding)
CREAT GROUP CORP.	Biotest AG (2017)	0.940

Source: Börsen-Zeitung, 26.01.2017: “China hat es in Deutschland schwerer” (China’s difficulties in Germany).

* The German government initially resisted the sale of the robot manufacturer *Kuka* to the private Chinese home appliance producer *Midea* in 2016. The takeover of the German semi-conductor company

Aixtron by China's *Fujian Grand Chip Investment Fund* was blocked by the United States on security grounds in late 2016.

Contrary to private equity partners who had owned some of these companies before, e.g. *Krauss Maffei*, the new Chinese owners pursue a long-term strategy, are not interested in a quick exit, and are prepared to provide favourable refinancing terms.

The Chinese owners can use their investment in leading European firms to improve their reputation on world markets, increasing export capacity and turning into a reliable trading partner. But the vice versa effect should not be underestimated either. Most of the Chinese firms are state-owned with a strong focus on domestic markets.

The challenge for companies such as *Krauss Maffei* in Germany, the *Port of Piraeus* in Greece or the steel mill *Zelezara Smederevo* in Serbia rests in expanding their new owners' understanding of the rules of the game on world markets to the domestic and regional conditions, be it in shipping, plastics manufacturing or mechanical engineering or road infrastructure.

China's ambition in Germany extends beyond the acquisition and investment drive. It also includes the construction and financing of a new rail freight route carrying Chinese manufacturers from the city of Zhengzhou overland through Russia to Hamburg, Germany where Europe's second largest commercial port is located (after Rotterdam, The Netherlands).

Financial Connectivity

The availability of financial resources by Chinese authorities forms an integral part of the Balkan Silk Road project. The primary instrument is lending at concessional terms to state bodies, public institutions and companies for infrastructure projects.

To what degree such lending can deepen multilateral and bilateral financial cooperation remains a matter of debate. It is early days to argue that it has enhanced coordination in monetary policy. What is taking place is the emergence of regional development financial institutions (see below). These initiatives seek to strengthen cooperation, but the monitoring and managing of financial risks is not yet a priority area.

To illustrate: In the course of the past decade, China has gradually established and facilitated the development of financial governance structures that can serve to support the BRI. This emerging financial architecture includes multilateral institutions such as the *Asia Infrastructure Investment Bank* (AIIB), the *New Development Bank* (NDB), and the *Silk Road Fund* (SRF).

The AIIB started operations in 2016. China's stake in the AIIB is 30 per cent, while its voting share is 28 per cent. But this voting share does *not* give China the capacity to veto projects. It should also be underlined that the AIIB does not only exist for China's benefit. As a newly established IFI, the AIIB currently has 56 founding members and 24 prospective members.

Britain, Germany and France are founding members of the AIIB, while the United States has so far refused to join the institution. Its headquarters are located in Beijing.

A host of Chinese commercial and specific (sectoral) policy banks further supplement this construction of financing channels, e.g. the *China Development Bank*³⁸ (CDB), the *Export and Import Bank of China* (EIBC), *Postal Savings Bank* (PSB) and the *China Agricultural Development Bank* (CADB). Many of these Chinese-led financial institutions are both cooperating with and competing against existing development banks, most notably the *Asian Development Bank* and the *World Bank*.

As regards financial cooperation between China and multilateral lenders headquartered in Europe, a web of financial connectivity is emerging. On the occasion of the BRI Forum in May 2017, six multilateral lenders signed an MoU to support China's Belt and Road Initiative. They include the *Asian Development Bank*, *Asian Infrastructure Investment Bank*, *European Bank for Reconstruction and Development*, the *New Development Bank*, the *World Bank*, and the *European Investment Bank*.

At the domestic level, the presence of financial institutions from China in southeast Europe is progressing at a slow pace. Overall, Chinese banks have so far hesitated to enter local markets in south-eastern Europe. The prevailing modus operandi is debt financing of investments through banks operating from China (or Hong Kong) rather than establishing a network along the Balkan Silk Road. Equity funding is slowly gaining ground, notably in Greece and Serbia.

A banking footprint is gradually being established. In the case of Greece, the *China Development Bank* (CDB) signed a memorandum of understanding (MoU) with the Bank of Greece in July 2016. In Serbia, the *Bank of China* opened a new branch in Belgrade in January 2017. Financial connectivity is also being facilitated by the creation of two Sino – CEE Investment Cooperation Funds, first in 2012 and most recently in 2016. The second of these funding channels has an initial investment capital of USD 11 billion, with a leverage ratio of one to five, seeking to raise 50 billion euros in project finance (see footnote 7).

People-to-People Bond

A further priority area concerns the promotion of exchanges and dialogues between different cultures and to heighten mutual understanding and traditional friendships to form the basis for the advancement of regional co-operation.

This people-to-people bond is all the more relevant when the arrival or subsequent surge of Chinese investments in BRI related countries raises concerns among domestic political authorities, collective bargaining organisations (e.g. trade unions) and civil society representatives. Put otherwise, in most initiatives it is China that intends to define the parameters of lending, employment impact (domestic or Chinese workers) as well as being a rule maker and less a rule-taker.

The feedback from domestic stakeholders engaged in the Balkan Silk Road project suggests that some see an uncomfortable role of junior partner in the Sino-Hellenic or Chinese-Serbian relationship. The economic, financial and diplomatic muscle that Chinese institutions bring to the table in south-eastern Europe add up to a sphere of expanding influence that sits uncomfortable with some domestic policy makers and observers.

The initial reaction by political authorities may be to try and protect specific companies, sectors and industries deemed “essential” in the national interest. In such circumstances, it is critical that Chinese investors focus on a set of exchanges and dialogues that include:

- Clear and transparent communication of business objectives in the proposed acquisition or investment transaction. This approach focuses on underlining the credibility of China’s ambitions and seeking to address potential misgivings about BRI;
- Address potential concerns about “fire sales” and “loss of know how” with arguments to the contrary, e.g. providing access to financial resources, improved trade options on Chinese markets, better operational perspectives for domestic businesses, job creation impact, etc.
- Provide in such people-to-people exchanges as much transparency as possible regarding financial dealings, procurement practices and why funding for infrastructure projects requires additional resources beyond what can be provided by the World Bank, IMF, EBRD or IPA assistance from the Commission in Brussels.

Appendix B:

List of interview partners in individual countries

Greece:

Mr Liu Jingdong, Public Diplomacy Director, Embassy of the People's Republic of China in Athens, Greece.

George Tzogopoulos, Researcher, *Hellenic Foundation for European and Foreign Policy* (ELIAMEP) as well as founder of <http://chinaandgreece.com/>, Athens.

Nick Malkoutsis, Founding Member of *Macropolis*, Athens.

Germany:

Lothar Altmann, Associate Professor at the UNESCO Department for International & Intercultural Relations, *Bucharest State University*.

Serbia:

Daniel Berg, Director, Head of Serbia, *European Bank for Reconstruction and Development*, Belgrade.

Peter Tabak, Lead Economist for Croatia, Serbia and Russia, *European Bank for Reconstruction and Development*, Belgrade.

Danica Milovanovic, Director, *Chamber of Commerce and Industry of Serbia*, Belgrade.

Nenad Durdevic, Director of the International Economic Relations Division, *Chamber of Commerce and Industry of Serbia*, Belgrade.

Predrag Bjelic, Professor, *University of Belgrade*, Faculty of Economics,

Sebastian Sosa, Resident Representative in Serbia, *International Monetary Fund*, Belgrade.

Marko Paunovic, Economist, *International Monetary Fund*, Belgrade.

Martin Knapp, Exekutive Director, *German-Serbian Chamber of Commerce*, Belgrade.

Lutz Kober, Project Director for Serbia and Montenegro, *Hanns Seidel Foundation*, Belgrade.

Klaus Fiesinger, Regional Director for south-eastern Europe, *Hanns Seidel Foundation*, Zagreb.

Bosnia and Herzegovina:

Ian Brown, Head of EBRD office in Bosnia and Herzegovina, Sarajevo.

Hamdo Tinjak, Secretary of the Ministry, *Ministry of Foreign Trade and Economic Relations*, Sarajevo.

Gazmend Turdiu, Deputy Secretary General, *Regional Cooperation Council*, Head of Programme Department, Sarajevo.

Prof. Fikret Čaušević, *School of Economics and Business*, University of Sarajevo.

Adnan Muminović, Political Economic Adviser, *Delegation of the European Union to Bosnia and Herzegovina and European Union Special Representative in BiH*, Sarajevo.

Michael Weichert, former head of regional office for south-eastern Europe, *Friedrich Ebert Foundation*, Sarajevo.

FYR Macedonia:

Christine Althausen, Ambassador, Federal Republic of Germany, Skopje.

Ljubomir Drakulevski, Dean of Faculty of Economics, Cyril and Methodius University, Skopje.

Nikola Naumoski, NGO representative, *The Balkan vive tour*.

Vasko Popetrevski, Journalist, Skopje.

Dragan Tevdovski, Minister of Finance, Skopje.

Milan Zivkovic, head of office, *Friedrich Ebert Foundation*, Skopje.

Endnotes:

¹ European Council on Foreign Relations, “China’s Investment Influence: The Future of 16+1 Cooperation”, *ECFR.eu China Analysis*, December 2016, [http://www.ecfr.eu/page/-/China Analysis Sixteen Plus One.pdf](http://www.ecfr.eu/page/-/China%20Analysis%20Sixteen%20Plus%20One.pdf).

² For full list of deliverables from the *Belt and Road Forum for International Cooperation* see http://www.chinadaily.com.cn/china/2017-05/16/content_29359377.htm.

³ Jens Bastian, “China - Greece: One Belt, One Road?”, *Macropolis*, 29.04.2015, <http://www.macropolis.gr/?i=portal.en.the-agora.2470&itemId=2470>.

⁴ *COSCO Shipping* is the owner of the world's fourth largest container fleet.

⁵ Following the Port of Piraeus acquisition Cosco Shipping is considering supplementing this move with an additional port investment in northern Greece. One candidate under consideration is the port of Alexandroupoli. The city in the region of East Macedonia and Thrace benefits from its position at the center of land and sea routes connecting Greece with Turkey and Bulgaria.

⁶ The first *Celestyal Cruise* ship carrying a group of Chinese tourists set sail from the Port of Piraeus in April 2017. The project took two years to finalize. Celestyal will also use the Greek port of Lavrio for home porting. It features Chinese crew members, cuisine and guides for the Greek sites.

⁷ See: “China Launches \$11 billion Fund for Central, Eastern Europe”, <https://www.reuters.com/article/us-china-eastern-europe-fund-idUSKBN13105N>.

⁸ See Chamber of Commerce and Industry of Serbia, unpublished policy paper: “Chinese Investments in CEE”, April 2017. The Chinese ambassador to Serbia speaks fluent Serbian.

⁹ In 2015 the Chinese company *Landbridge Group* bought a 99-year lease on the port of Darwin on Australia’s northern coast.

¹⁰ See European Commission, Directorate-General, Trade in Goods with FYR Macedonia, page 8, http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113381.pdf.

¹¹ See Sinisa Jakov Marusic, ‘Macedonia Buys New Trains from China’, *Balkan Insight*, 25. June 2014, <http://www.balkaninsight.com/en/article/macedonia-buys-new-trains-from-china>

¹² See European Commission, Directorate-General, Trade in Goods with Bosnia and Herzegovina, page 8, http://trade.ec.europa.eu/doclib/docs/2008/august/tradoc_140028.pdf.

¹³ See <http://www.balkaninsight.com/en/article/china-opens-new-belgrade-bank-as-balkan-hub-01-27-2017#sthash.VNpSJxoq.dpuf>

¹⁴ See <http://www.balkaninsight.com/en/article/serbia-s-credit-based-economic-cooperation-lacks-direct-investments-06-14-2016>

¹⁵ See European Commission, Directorate-General, Trade in Goods with Bosnia and Herzegovina, page 8, http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113358.pdf.

¹⁶ See more at: <https://www.seenews.com/news/bosnias-epbih-seeks-govt-guarantee-for-chinese-loan-for-tuzla-tpp-project-554235#sthash.V5fMhyWP.dpuf>

¹⁷ There is some need for clarification about this co-financing element from a state-owned company. Some observers argue that it is subject to an inquiry about state aid rules. This would also further explain the long delays in any decision-making process.

¹⁸ See „Changing with the Region. RCC Strategy and Work Programme 2017-2019“, RCC, Sarajevo, Year III, No. 3, p. 5.

¹⁹ Policy makers in BiH lament that major cross border infrastructure bypass the country, such as the *Transadriatic Pipeline* (TAP) and *Southstream*. This is seen as a major impediment to attracting higher volumes of investor interest, from Russia, Turkey and EU countries. Equally, the absence of EU Candidate Status for BiH further contributes to these “branding or marketing issues”.

²⁰ See *European Council on Foreign Relations*, ‘China’s Investment in Influence: The Future of the 16+1 Cooperation’, ecfr.eu, December 2016, p. 6.

²¹ See Patrick Blagrove and Esteban Vesperoni, “Spillover Implications of China’s Slowdown for International Trade”, Spillover Task Force, International Monetary Fund, September 2016, No. 4, p. 1.

²² See *Financial Times*, “Cosco Shipping buys controlling stake in Spanish port for €203m”, 13. June 2017, <https://www.ft.com/content/26c99549-29d4-3d00-8714-e62d22e83bcf>.

²³ Chinese investments in European ports is not matched by European access to Chinese ports. Not a single Chinese port is majority-owned by a European company. But COSCO is increasingly becoming the majority owner of various European ports. See Ben Bland, “Acquisitive Beijing Sets Course for Shipping Dominance”, FT, 18th July 2017.

²⁴ Lawrence Summers, “Put American Foreign Policy Back on the Pitch”, *Financial Times*, July 6th, 2014.

²⁵ Frans-Paul van der Putten (ed.), Francesco Saverio Montesano, Johan van de Ven and Peter van Ham, „The Geopolitical Relevance of Piraeus and China’s New Silk Road for Southeast Europe and Turkey“, *Clingendael Report*, December 2016, https://www.clingendael.nl/sites/default/files/Report_the%20geopolitical_relevance_of_Piraeus_and_China%27s_New_Silk_Road.pdf.

²⁶ See e.g.: ‘China’s Investment Influence: The Future of the 16+1 Cooperation’, *European Council on Foreign Relations*, December 2016.

²⁷ See “EBRD Updates Transition Concept”, November 2016, <http://www.ebrd.com/news/2016/ebrd-updates-transition-concept-.html>

²⁸ See Martin Sandbu, ‘Europe Must Respond to China’s Belt and Road Initiative’, *Financial Times*, May 16, 2017, <https://amp.ft.com/content/1edf0d68-3a1e-11e7-821a-6027b8a20f23>.

²⁹ Such a critical assessment is starting to be voiced – albeit in careful terms – by Chinese sources themselves. In early 2017 a report circulated in Beijing with the title: “The Reform Obstruction Phenomenon”. It was written by researchers from the Economic System and Management Institute of China’s National Development and Reform Commission. This Commission steers policy on industry, energy and many other sectors, domestic and abroad.

³⁰ India has been resistant to getting on board. Delhi has objections to those aspects of BRI that risk to impinge on its national sovereignty. Tokyo is wary of being seen to play a ‘subordinate’ role in any Chinese master plan, despite its reliance on trade with China.

³¹ In December 2015 China’s President Xi attended a meeting of African leaders in Johannesburg. He offered extensive lending contracts and the following description of his government’s activities in Africa: “China supports the settlement of African issues by Africans in the African way” (quoted according to: Eswar Prasad: “China Takes Aim at West’s Global Clout”, *The New York Times* (International Edition), 02.09.2017.

³² See <https://www.bloomberg.com/news/articles/2017-05-04/china-s-belt-road-plan-may-top-500-billion-credit-suisse-says>.

³³ See “China ‘New Silk Road’ investment fell in 2016, despite policy push. Xi Jinping’s signature initiative faces headwinds as politics and profit collide”, in *Financial Times*, <https://www.ft.com/content/156da902-354f-11e7-bce4-9023f8c0fd2e>.

³⁴ The World Bank’s *International Comparison Program* measures the size of a country’s economy based on purchasing power parities. On that basis, China overtook the United States as the world’s largest economy in 2014.

³⁵ See Angela Stanzel, ‘China’s Belt and Road – New Name, Same Doubts’”, *European Council on Foreign Relations*, 19th May 2017, http://www.ecfr.eu/article/commentary_chinas_belt_and_road_new_name_same_doubts

³⁶ While India boycotted the event completely, Japan only sent a representative (the secretary general) from the Liberal Democratic Party of Japan to the BRI Forum.

³⁷ So far 18 EU member states have joined the AIIB.

³⁸ The most active financial institution to date (in terms of loan exposure) is CDB with more than 900 financed projects in 62 countries and committed lending exceeding 800 billion US dollars (see *Kathimerini*, 25th February 2017, “Μια Ζώνη, Ένας Δρόμος» και πολλές συνεργασίες” (“One Belt, One Road” and Many Co-operations”).