HUNGARIAN – CHINESE RELATIONS: FOREIGN TRADE AND INVESTMENTS

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FDI investment cannot help mitigate the huge gap in foreign trade between the two countries. In the last years the Hungarian deficit in bilateral trade continuously increased. Hungary could not reach surplus even in agriculture. While a regional leader in incoming FDI, Hungary is still negligible from the point of view of China.

Key words: China, Hungary, bilateral trade, deficit, new commercial way
JEL: F10, F50

1 BILATERAL TRADE

The first trade and shipping contract with China, in which Hungary was also a partner, was signed by the Austro-Hungarian Monarchy in Beijing in 2nd of September in 1869. It was valid until 1917. Shortly after it came into force the Monarchy opened a General Consulate in Shanghai and in 1897 in Beijing too. The Monarchy's presence in China strengthened after it took part in the suppression of the riot in 1900 and it got concession area in Tianjin where a Consulate was also opened. Fortunately the relationship stayed bilateral and in 1902 China opened a representation. Four years later a delegation led by a Manchu prince visited the Monarchy; they were followed by other prince in 1910. As a result of the visits the two empires signed seven loan agreements.

During the First Word War, in 1917, diplomatic relations were interrupted for a long period of time, because China declared war on the Monarchy. They concluded a peace treaty only in 1926. The new period in the relationship started after the Second Word War, when China and Hungary became part of the same global political block. Shortly after its declaration, Hungary recognized the People's Republic of China and the two countries reestablished diplomatic relations, which helped foreign trade between the two economies. (Salát, 2009) In the period after the Cultural Revolution the two countries drifted away from each other and relationship got back to normal only after 1978, when reforms started in China, and its leaders interested in the Hungarian New Economic Mechanism.

In the first period (1949-1990) relationships were influenced by politics, while in the second period, after 1990 trade relations depended on economy. Despite Hungary's regime change, the relationship stayed stable and well-balanced, but it did not intensified. Trade relationships also improved, and nowadays China is the fifth most important import partner, while it ranks fifteenth as an export destination.

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China is the second largest trade partner for Hungary outside European Union after Russia and Hungary is the third main partner for China in the Central European region after Poland and the Czech Republic.

The first main meeting in the second period was in 1991 when Chinese Secretary of State visited Hungary, than in 1994 when President of Hungary Árpád Göncz traveled to China, which was crucial for the relations. After visits the bilateral meetings became regular in order to deepen relations. When the Chinese Secretary of State visited Hungary the two countries signed an investment protection treaty, in the next year a treaty against double taxation of incomes and a preventative agreement about tax evasion. Moreover, in that year China opened a Commercial Center in Budapest. As the relations deepened, Hungarian governments decided to set up a special government committee which deals specifically with Hungarian-Chinese relations.[2] (Német, 2013)

In 2003 the Hungarian Prime Minister and his delegation also visited China; it was a short but very successful trip. Peter Medgyessy had discussions with the Chinese Premier, with the State President and with the Chairman of the National People's Congress Standing Committee. The visit was also a special political event. This was not only a political trip but it was a gesture as well in order to rebuild the confidence. To further strengthen this confidence and relations in general, on 19th of April, 2004 there was the meeting of the Hungarian-Chinese Joint Economic Committee in Beijing. The discussion was not only about economical but also political issues. Beside of the meetings Embassies were also expanded and new representations were established.

In 2006 the 11th Chinese Five Year Plan came into force, which determined new fields of the cooperation. This plan was an opportunity for Hungary as well, because the Chinese leadership wished to improve technology in industry and in environmentally friendly agriculture. These aims opened new ways for Hungarian agriculture, in product level and also in technological level. In this year there were two considerable events as well: China Hi-Tech Expo and Style Hong Kong[3] were organized in Budapest.

In 2007 the 'Hungarian Season' event took place in China, which was not only an economic, but also a touristic and cultural event. Economical programs helped to provide knowledge about the Hungarian economy and investment environment. It gave also support to business meetings and indirectly provided an opportunity for Hungarian enterprises to become suppliers during the Olympic Games in Beijing. 2008 was not only success for some enterprises but also was success for political relationship. There were many meetings between the two parties.

2009 was the 60th anniversary of the diplomatic relations and in this year China was the guest of honor at Budapest's International Fair. In this year an agreement was concluded between the Chinese Stock Exchange and ITD Hungary, which supported Hungarian SMEs to create partnership with Chinese partners. (Szunomár, 2010)

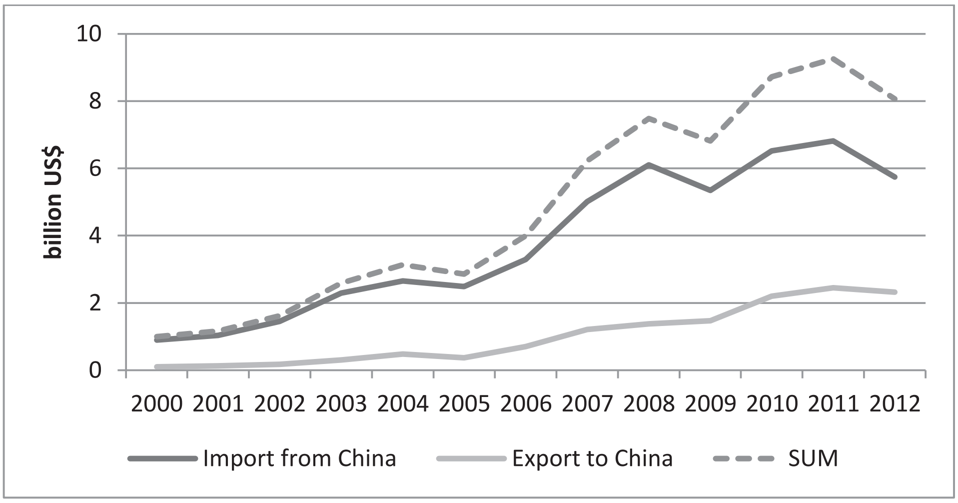
After the Hungarian elections of 2010, the policy of 'Opening to the East', which naturally includes China, became a priority for the new Hungarian government.

[2] Hungarian Consulate General, Shanghai, China.
[3] An exhibition of products that are essential for modern lifestyle.

Hungary has a trade relationship with almost every Chinese province and city, but the main partners are Beijing, Guangdong, Zhejiang, Guangxi, Jiangsu, Shanghai and Tianjin.

Similarly to other member states of the European Union, Hungarian foreign trade with China has increased in the last two decades. China's WTO membership has had a positive effect. Not only has trade volume increased for the whole EU and also in Hungary, but also the deficit, as it is shown in the first diagram. After 2003-2004 trade volume (more exactly import from China) increased quite fast. During a decade after the millennium, it increased tenfold. (Figure 1)

Figure 1: Foreign trade volume between China and Hungary



Source: MOFCOM of the PRC

Chinese exports have been significantly higher than imports, but Hungary could achieve significant increase in absolute terms, and in spite of the world economic crisis it was able to expand its exports to China in 2009, while world trade shrank during that year. The entire value of trade was 6.81 billion US$, from which Hungarian export was 1.47 billion US$. Compared to the previous year this was 6.5% increase, while Hungarian imports from China decreased by13%.[4] This year was the first year during the analyzed period when Hungarian deficit was smaller compared to the previous year. Similar developments took place in 2012 as well, Hungarian imports decreased by 11% in USD terms, however the value of exports increased by more than 7%. The reason for the high deficit is multinational companies and their division of labor; therefore on bilateral level countries cannot take measurements so easily for a better balance. (Matura, 2013)

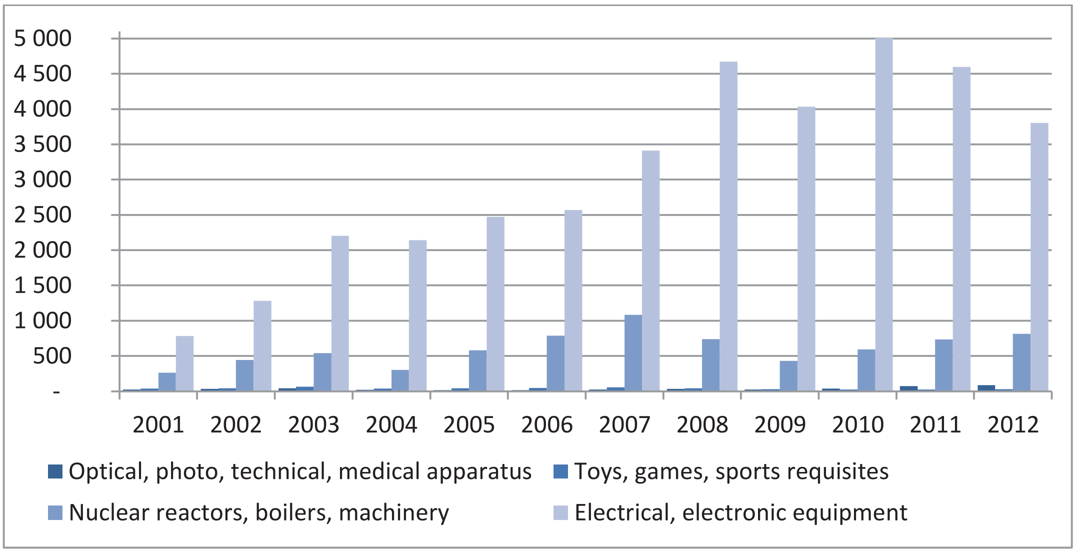
The structure of the bilateral trade is quite similar; the main products are motor vehicles and its parts, electronic and telecommunication equipment. But let us see import and export side in details. In 2013 China was the the fifth largest imports partner for Hungary after Germany, Russia, Austria and Slovakia. The number of export commodities exceeds 1900 items, and import commodities 650 items. The main import products are electrical and electronic equipments, which are followed by machineries, mobile phones, medical optical instruments. Organic chemicals, toys and games, footwear and

[4] It has to be noted that the available data sources on Chinese-Hungarian bilateral trade are ambiguous, there are significant differences between Chinese and Hungarian data from year to year.

furniture also feature, but these values are much less than the two main categories. In spite of widely held beliefs to the contrary, textiles and cloth apparels are only 0.6% of overall imports.

When the crisis erupted in 2009, all products categories saw a decrease. However, by 2010 there was some increase. After that, imports could not reach the value of the previous year[5], which did not depend on China but on Hungary.[6] The biggest decrease happened in not so important import products like products of animal origin; mineral fuels, oils, distillation products; explosives, pyrotechnics, matches, pyrophorics.

Figure 2: Main import commodities from China to Hungary (in million US$)



Source: OECD Statistics

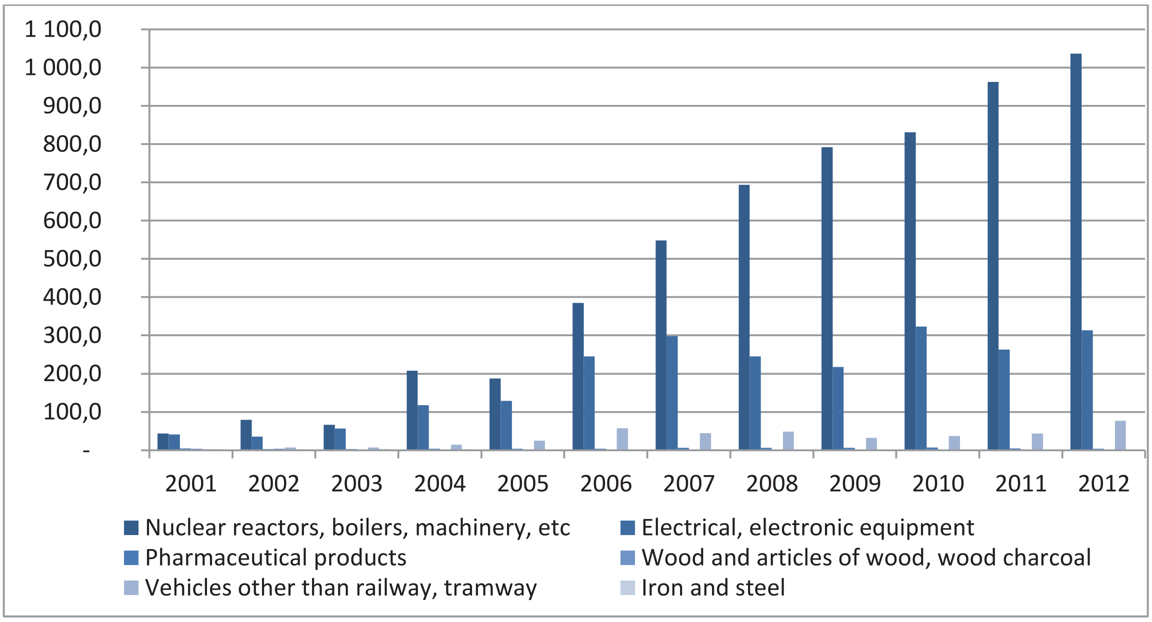
If we take a look at the surrounding countries' imports, we can see similarities to the effect that imports mostly contain manufactured products, transport equipment and other machineries (of course at a different rate).

Hungarian exports to China, like imports, increased significantly in the last decade. Export consist mostly of machinery and electrical machinery products. These products are exported by the largest European multinational companies which have subsidiary companies in Hungary. They include AUDI, Siemens, IBM, Allison and Microsoft (earlier Nokia). (Thai Trade Center Budapest, 2012) The biggest increase can be seen in vehicles (except railway, tramway), whose value was 31 fold higher in 2012 compared to the millennium. (Figure 3) The reason is the increasing production of the above mentioned multinational car companies. The biggest drop since 2000 took place in not so high-volume products: in furniture, lighting, signs, prefabricated buildings.

[5] 2008/2009 – 81%; 2009/2010 – 125%; 2010/2011 – 98%; 2011/2012 – 89%. (OECD Statistics)

[6] Whole Hungarian import decreased in the last five years and the country had and still have surplus in foreign trade.

Figure 3: Main exports commodities from Hungary to China (in million US$)



Source: OECD Statistics

There are many factors that can influence the future trade volume and value: the world economy, world political situations, the domestic economy and domestic politics. But if we suppose that everything will be stable in the next years, then Hungarian import from China will reach 10 billion US$ in 2019 while Hungarian export to China will be 5 billion US$. Hungarian export will increase faster in percentages, but in value the gap between export and import will increase in favor of China.

On the import side the ratio of electrical and electronic equipments will increase faster than machineries. The value of machineries will achieve 1 billion US$, and the value of electrical equipment will exceed 8 billion US$ by 2019. The value of optical, photo, technical and medical apparatus will also increase: during the next 5 years it will double. Some import products will almost disappear: toys, games and footwear, gaiters. Toys and games have been the third main import commodities, but their value is decreasing from year to year as well as footwear and gaiters, as it can be seen in the first Annex.

On the export side the two main products are also machineries and electronic equipment. The value of the first one will exceed 2 billion US$ already by 2018, and the second one will exceed half a billion US$ by 2017. Vehicles are likely to remain the third most important export commodity, but their ratio in overall export will slightly decrease thanks to the developing car industry in China. More and more multinational car companies have subsidiary companies in China, mostly because of the lower wages, and thus vehicles are manufactured in the target country. Main export products include pharmaceutical products, whose ratio significantly increased in the last decade, except in the years of the crisis. Their value will be above 70 million US$ in the upcoming two years. Wood and articles of wood will show hectic changes in the next years, because their value depends on volatile demand. If we can believe in trends, two commodities will almost disappear from Hungarian exports: iron and steel, as demand for them continuously decreases. The data are summarized in the second Annex.

There is no lack of political will. In the last years numerous agreements have been signed, but the Hungarian economy is too small for China. The demand is large but supply is not. Hungarian enterprises, producers have not got enough capacity to fulfil it. China favours Hungary as a gateway to Europe through foreign direct investment, since if at least 50% of the products are produced in the EU, it becomes a European ware. But FDI investment cannot alleviate the huge gap in foreign trade between the two countries.

More optimistic points of view also exist. András Inotai and his colleagues can see opportunities in partnership in agriculture, where Hungary still has a deficit. China is the world's largest producer of agricultural products, but it has also has serious production and supply problems. If Hungary could strengthen its exports and exports structure, new co-operations could be carried into execution mostly in the field of technologies like drought resistant crops, production practices, food safety, grape processing and wine production. Further opportunities exist in 'knowledge-export': research and development. Inotai and his co-authors see possibilities in 'knowledge sale' because the first priority for China is investment into human factor on which modernization depends. (Inotai-Juhász, 2009)

Matura (Matura, 2013) warns that according to his estimates some 91.24% of Hungarian exports to China are made up of the exports of multinational enterprises active in Hungary. Quite a lot of that might actually be intrafirm trade. As far as imports are concerned, the popular image of Chinese imports to Hungary consists of clothes and shoes. According to Matura, in fact they make up no more than 0.7%. Some 85.4% are machines and vehicles. A very significant part of imports might also be intrafirm trade, components that are re-exported after assembly in Hungary, especially in the electronics sectors.

2 NEW COMMERCIAL CHANEL FROM CHINA TO MIDDLE-EUROPE

The transport connection between the northern Adriatic ports and Central-Europe through the Western Balkans is one of the major importance for the regions in Central and South East Europe. Besides the efforts set for developing the Trans-European Networks, actions have to be defined to provide efficient connections between and to the main transport corridors for example the Chinese goods. These connections are one of the major importances for the regions which are not directly linked to these corridors. The new planed corridor will provide an efficient railway connection on existing tracks between Central Europe and the North Adriatic Ports connecting Rail Network Europe (RNE) Corridors 7, 8, 10 and 11. The improvement of international accessibility is strongly connected to the increasing inner-regional connectivity, but it is also important for new hinterland connection with the Northern Adriatic ports Koper and the only Adriatic deepwater, Harbour Rijeka. The establishment of the upgraded TEN-Axes 17, 18, 22, 23, 25 (as well as the planned possible enlargement of Russian broad gauge railway) find their intersection in the Vienna/Bratislava region and build a transnational hub in this region. The planed railway corridor is an interconnection among this transnational hub, Balkan countries, the Northern Adriatic ports of Rijeka and Koper as well as the corridors to Eastern Germany. It will focus on upgrading of already existing rail infrastructure (with moderate investment costs) and the connection to all other means of transport.

Is it not the only a project dealing with the development of the transport system, but also with cooperation between existing projects and initiatives dealing with similar topics and highly perspectives commercial way for the Chinese goods.

2. 1 Main objective

Implementation of measures for the **improvement of accessibility and logistic workflow** as a basis for regional development in South East Europe:

a) Better accessibility as basis for **regional economic growth** in South East Europe
b) Develop **environmental friendly freight transport** (green corridors)
c) Improve (economic) **cooperation** between Central and South East European regions
d) Access **alternative financing options** for the necessary improvement of transport infrastructure
e) Create a **common interest** between and within the partner regions
f) New possibility for the **chines investment capital**

3 INVESTMENS

Due to large scale Chinese export profits and savings, enormous amounts have been flowing into the Chinese banking system. Together with state regulation, these have led to very low (often negative real) interest rates. Naturally, this has caused an excess supply of capital and a strong propensity to lend (the negative effects of which are already felt across the country). This capital no longer restricts itself to China, but is also seeking opportunities abroad.

As it is well known, the Chinese government has been seeking a reorientation of its strategy on foreign financial markets in recent years. There has been a shift away from purchasing (mainly Western) government debt, replaced by investment into the real economy. It is little known that since 2011 the PR of China essentially no longer finances United states borrowing, which had been a central element of the global economy earlier. At the same time investments by Chinese firms and state investment funds are estimated to have reached some USD 90 billion in 2012. The time is nearing when China will no longer be a net recipient of investment, but a net investor. It is hard to follow the precise global distribution of Chinese ODI, only estimates are available. The picture is further complicated by the fact that some 75 per cent of Chinese overseas investment is channelled through tax havens such as the Cayman Islands, the British Virgin Islands and Hong Kong[7].

As far as Chinese investment in Central and Eastern Europe is concerned, the largest stock of it in the region, approximately USD2.5 billion, is to be found in Hungary. However, this stock is extremely concentrated. About three quarters of it are connected to a single deal, the Chinese acquisition of the Borsodchem chemical corporation. (Matura, 2012) In recent years there have been numerous proposals for investments, which have not materialised. Some investments are frozen (citric acid and solar panel plans), others have not even taken off (Debrecen industrial park, cargo airport).

There were proposals for Chinese investments into the renewal of major terminal railway stations in Budapest, as well as a railway link between the Western Railway Station and Budapest Liszt Ferenc

[7] 2010 Statistical Bulletin of China's Outward Foreign Direct Investment. Beijing: Ministry of Commerce of the People's Republic of China, 2011. Electronic version: http://hzs.mofcom.gov.cn/accessory/201109/1316069658609.pdf.

International Airport. These have also not materialised. Negotiations related to Chinese acquisition of the bankrupt Hungarian national air carrier, Malév, have also ended without success.

There has also been media speculation about the Chinese purchasing of Hungarian government bonds. Little can be known about how much this has materialised, not least because – as we have already mentioned - the implementation of Chinese overseas investment comprises a state secret. At the same time the fact that China has made an offer of no more than one hundred billion euros for the entire European Union, we can conclude that the sum aimed at Hungary cannot be overly significant. According to analysts, Hungary's external borrowing requirement was about two thousand billion forints, which was about ten billion dollars. This was significantly higher than the financial aid China was read to provide the EU. (Matura, 2012)

4 Resolution of potential investment disputes

Due to the low value and the high concentration of investments, the resolution of investment disputes has not been a major issue so far. More important are the factors that restrict the increase in investments.

A major obstacle is the absence of direct flight connections between the two countries, as well as the difficulties related to issuance of visas. Hungary still has a relatively dispersed network of state organs responsible for receiving Chinese investment.

There have been successes in cultural relations. Three Confucius Institutes have opened in Hungary, in Budapest, Szeged and Miskolc. The Hungarian Cultural Centre was opened in Beijing in 2013, but an adequate budget for the centre is still not guaranteed.

Educational and research cooperation is rather one sided, as the Hungarian higher education and research sector, which suffers from continuous underfinancing, is unable to respond in most cases to Chinese initiatives.

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