

Hungary's 'opening to the East' as China's 'good friend'

The 'Opening to the East' is an economic strategy that was announced in 2010 after the Fidesz-KDNP coalition gained a constitutional majority in parliament, and which the government in Budapest has consistently pursued since then. It is aimed at reducing Hungary's trade and industrial dependence on the West in favour of closer cooperation with Russia, Turkey and countries in the Far East, mainly China. At the ideological root of the 'opening to the East' is Viktor Orbán's personal conviction that the West's civilisational dominance is coming to an end, and Hungary thus needs to strike a balance between its relations with China on the one hand and its European allies & the US on the other. In his own words, his broader strategy amounts to a 'peacock dance', or the political courtship of multiple parties.

During his thirteen-year rule, the Hungarian prime minister has repeatedly voiced his appreciation for China's economic achieve-

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ments while overlooking issues such as unfair trade practices and human rights violations. In recent years Hungary has become the main defender of China's interests and an advocate for it in the EU arena: between 2016 and 2022, it used its veto power six times to block the EU Council's decisions condemning China's actions.¹ It has also repeatedly opposed initiatives that would undermine China's economic position: for example, in December 2023, it refused to sign the European Wind Charter which calls for the EU's wind industry to be protected from the unfair practices of Chinese manufacturers. The Hungarian prime minister has been careful to avoid antagonising China, and has used his good relations with it as a bargaining chip inside the EU.

While the European Union has been growing sceptical of cooperation with China, which is increasingly seen as a 'systemic rival', Hungary has taken the opposite stance and advocated closer relations with it. In February this year, on the occasion of the 75th anniversary of the establishment of diplomatic relations between the two countries, Hungary became the first EU and NATO country to sign an agreement with China to cooperate in the area of 'public security'.² In addition, it has been developing bilateral relations with China through the '14+1' format and the Belt & Road Initiative. While the Central and Eastern European countries have been gradually downgrading their participation in the '14+1' summits, Orbán has attended all of the platform's nine meetings. Similarly, he refused to join the unofficial EU boycott of the 2023 Belt & Road Forum in Beijing, which was linked to Vladimir Putin's presence. Orbán was the only leader from the EU to attend that event and meet the Russian president.³ According to Hungarian foreign minister Péter Szijjártó, Hungary's cooperation with China presents "more opportunities than threats", while his Chinese counterpart Wang Yi has declared that relations between the two countries are in their "best period ever".

From China's perspective, Hungary is a "good friend and companion who has stood the test of time".⁴ Indeed, it has been seeking to forge closer relations with China despite the developments inside the

¹ R.A. Wessel, V. Szép, *The implementation of Article 31 of the Treaty on European Union and the use of Qualified Majority Voting. Towards a more effective Common Foreign and Security Policy?*, Brussels, November 2022, p. 64, europarl.europa.eu.

² While the details of this agreement have not been disclosed, it reportedly includes provisions to strengthen security and law enforcement capacities under the Belt & Road Initiative, as well as to combat terrorism and transnational crime. The agreement also allows Chinese police officers to be stationed in Hungary; according to the Hungarian government, they would be mainly present at tourist sites. We should assume that the Chinese government's primary concern is to monitor the Chinese citizens living in this country, who currently number around 18,000.

³ See A. Sadecki, 'The Orbán–Putin meeting in Beijing: Hungary drifting away from the West', OSW, 19 October 2023, osw.waw.pl.

⁴ The meeting between Hungary's Prime Minister Victor Orbán and China's Minister of Public Security Wang Xiaohong; see '匈牙利总理欧尔班会见王小洪', Xinhua News, 18 February 2024, gov.cn.

EU and pressure from the US. Hungary's consistently pro-Chinese policy has made it increasingly attractive as a location for Chinese investments, especially in areas which are politically risky or controversial in Europe. For example, in recent years it has become the largest logistics and manufacturing base for Huawei Technologies outside China. Despite strong pressure from the United States and warnings about Huawei's cooperation with the Chinese intelligence services, Hungary has refused to halt its cooperation with the Chinese telecommunications company on the development of a local 5G network.⁵ Hungary aims to act as a regional logistics hub for China thanks to investments such as the modernisation of the Budapest-Belgrade railway line and the Záhony transshipment terminal. However, China's investment activity in Hungary to date has exacerbated the Hungarian economy's structural problems. Indeed, the country has become a 'Chinese assembly plant': it is only involved in the manufacturing process, which does not entail any transfer of know-how or include local sub-suppliers, resulting in low added value of production for the Hungarian economy.

For China, the closer ties with Hungary provide an opportunity to mitigate the negative effects of its increasingly fraught relations with the European Union and to

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build a 'European bridgehead' for its economic and academic presence. Against the backdrop of the anti-subsidy investigation into the imports of Chinese electric vehicles which the European Commission launched in September 2023, the production of these cars in Hungary could help China avoid possible punitive tariffs and enable it to compete more effectively with European brands. Similarly, the stable relationship with Hungary has allowed Chinese research centres to expand their presence. Since 2017 Budapest has hosted the China-CEE Institute, which is *de facto* the only European representative office of the China Academy of Social Sciences, a state-owned research institute under the State Council of the People's Republic of China. China's Fudan University also planned to open its first overseas branch in Budapest, but that project was eventually put on hold due to resistance from the capital's mayor, who represents the opposition; the campus's future now largely depends on the results of local elections scheduled for mid-2024.

The first decade of cooperation: a lot of hype, little substance

The first decade of Chinese-Hungarian cooperation as part of Hungary's 'opening to the East' has been marked by high-profile projects in the infrastructural, automotive and digitisation sectors. However, their implementation has run into many difficulties. One of the two countries' flagship joint ventures is the construction of a 160-kilometre-long section of a high-speed Budapest-Belgrade railway line that was launched in 2014. It is eventually intended to link Hungary with the Greek port of Piraeus, which is managed by the Chinese shipowner COSCO; in the government's narrative, this would make Hungary the 'gateway to Europe' for Chinese goods. The project, which is part of China's Belt & Road Initiative, is worth around \$2.5 billion; around 85% of this sum has come from a loan that the EXIM Bank of China has provided to the Hungarian government. The railway's Serbian section (Novi Sad-Belgrade) went into operation in March 2022, but the Hungarian section is still incomplete; the government now says it will be finalised in 2025. According to the Hungarian government's forecasts from 2017, its investment in the Budapest-Belgrade rail project was expected to pay for itself within 10 years thanks to the projected increase in container traffic from China via the port of Piraeus.

⁵ In October 2023, the Hungarian telecommunications company 4iG, headed by the Orbán-linked entrepreneur Gellért Jászai, signed a separate agreement in Beijing with Huawei which provided for cooperation in the development of 5G and mobile communications, fixed networks and technical studies. A month later, PM Orbán and minister of economic development Márton Nagy visited Huawei's main headquarters in Shenzhen, where they signed a memorandum of understanding to strengthen the strategic cooperation that began in 2013.

However, in the project's early stages the independent media published alternative calculations: the Index news website estimated this period at 130 years,⁶ while Telex put it at 979.⁷

The difficulties with the construction of the Belgrade-Budapest link are typical of Chinese-Hungarian cooperation on major projects.

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In this case, the main problem is

the Chinese subcontractors' lack of competence to develop train control systems that would be compatible with European ones (ETCS). In addition, Hungary has found itself at loggerheads with the European Commission due to its failure to comply with the EU's public procurement law, resulting in further delays to the project. Hungary's financial problems are another obstacle. In Budapest's narrative, financing from China offers an alternative to funds obtained from the EU. However, this has mainly consisted of loans to the Hungarian state, which has placed a burden on its budget in contrast to the largely non-repayable EU funds. Inflation and shortages of construction materials have further increased the project's real cost, which has led to growing public doubts about its economic viability.

The Hungarian government's close ties with China have also triggered domestic tensions. For example, the plan to build Fudan University's campus in Budapest, the first such foreign branch of this prestigious Shanghai-based university, has become a bone of contention between the government and the opposition. The project's suspension formally stemmed from concerns raised by Mayor Gergely Karácsony that the campus would occupy large areas of city-owned land, but the main arguments in the debate have highlighted fears of China's rising influence in Hungary, disquiet at the resulting intelligence threat, and the more general problem of underfunded higher education. On the issue of the Hungary Fudan University project, the public has strongly supported the opposition's stance, as demonstrated by the wave of street protests that swept through Budapest in 2021. A poll conducted at the time by the independent think tank Republikon showed that two-thirds of Hungarian people rejected the idea of setting up a branch of the Chinese university in Hungary; a third of Fidesz supporters also disapproved of it.⁸

Other stalled projects include a high-speed railway to link the Budapest Nyugati railway station with the Ferenc Liszt airport, which a Chinese contractor was supposed to build, and China's planned purchase of Hungarian sovereign bonds to reduce the latter's public debt and speed up the implementation of joint projects, something that Chinese prime minister Wen Jiabao pledged back in 2011.

Likewise, China did not become the dominant investor in Hungary in 2010–21. Looking at the cumulative value of foreign direct investment (FDI), it is clear that the surge of Chinese capital which had been promised for a decade failed to reach Hungary until 2022. According to data from the National Bank of Hungary and Eurostat, China accounted for just 3.7% of all foreign investment in Hungary up until 2021. Among the EU's member states, Hungary actually had the highest percentage of Chinese investments, but their total value of €3.5 billion put China far behind the largest investors: German FDI totalled €25 billion during this period.

We should bear in mind that Hungary and China have failed to implement many of the projects they have announced with much fanfare in government statements and the media since 2010. The reason for this is difficult to identify, mainly due to the low transparency of their joint ventures. The successful ones include the Wanhua Chemical Group's takeover of BorsodChem, Hungary's debt-ridden second

⁶ '130 év alatt térülhet meg a méregdrága kínai vasút', Index, 1 December 2017, index.hu.

⁷ A. Kalmán, A. Curić, 'Budapest–Belgrád: a 979 év alatt megtérülő vasútvonal', Telex, 26 November 2021, telex.hu.

⁸ 'A Fudan Egyetem budapesti kampuszának támogatottsága', Republikon Intézet, May 2021, republikon.hu.

largest chemical company, in 2011 (although talks on this issue had already begun before Orbán took power), the establishment of Huawei's European logistics centre in Budapest in 2013, and the construction of BYD's electric bus factory in Komárom in 2016.

A chance for a breakthrough in the field of e-mobility

The only area where Hungary's 'opening to the East' appears likely to yield tangible results is the electric car sector. Global demand in this industry, coupled with the technological potential of Asian manufacturers, has given Orbán the long-awaited palpable benefits from his relationship with China. Hungary has become the beneficiary of two Chinese mega-projects: a factory of CATL, a lithium-ion battery manufacturer, and a car factory of BYD. Batteries for electric cars, which in Hungary are mainly manufactured by Chinese (and Korean) companies, have become a rapidly growing export commodity for the country.

The construction of an EV battery factory near Debrecen, which began in 2023, marked an investment breakthrough in Chinese-Hungarian relations. China's CATL, the

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world's largest producer of batteries for electric cars, is responsible for this project, which has an estimated value of €7.3 billion, Hungary's biggest-ever foreign investment. The project has stirred up controversy, becoming a target of protests from the local community and criticism from the Momentum and Our Homeland opposition parties which have demanded a referendum while highlighting its numerous environmental risks. Hungary has liberalised its environmental legislation to suit the low standards of Chinese investments, which has raised objections from the EU.⁹ According to the Hungarian Ministry of Foreign Affairs and Trade, foreign investment in e-mobility-related production in Hungary between 2016 and 2022 totalled €5.3 billion. Unofficial reports have also suggested that China will build its own solar power plants in Hungary (at an estimated cost of more than €2 billion) in order to provide stable sources of energy for its battery and electric vehicle factories.¹⁰ Hungary has offered numerous incentives for Chinese capital, including state subsidies (10–12% of the value in subsidies and tax breaks) and facilities such as improved land for construction with completed access routes. It has also encouraged business to invest in Hungary by aligning working hours with the vehicle production cycle (a controversial amendment to the labour code as part of the so-called 'slave law' of 2018) and providing guarantees of discretion (sensitive legal acts relating to investments are kept secret for 10 years).

The construction of an electric car factory in Szeged, which BYD announced in December 2023, will be the next major Chinese investment in the e-mobility sector. The Hungarian government will provide financial support for this project, but the amount of the assistance it gives will only be revealed once the European Commission has approved it. The decision by BYD, the industry leader in China, was driven by the steps taken by its competitors, including the expansion of Tesla's Gigafactory near Berlin, as well as the EU's announcement of an anti-subsidy probe targeting car imports from China. In fact, BYD already has a presence in Hungary: it has been making buses in Komárom since 2017. Low price is expected to be the main selling point of the cars that BYD assembles in Hungary: the manufacturer's statements have suggested that its cheapest Seagull model could cost only €9000.

⁹ According to reports from August 2023, the European Commission will review the merits of the environmental approval due to the project site's proximity to a NATURA 2000 protected area and the possible breach of the EU's water directive.

¹⁰ 'Orbán more likely to solve Hungary's energy troubles with China than Russia' [in:] S. Panyi, 'Goulash: Orbán's weeks of crisis; Ján Kuciak remembered', VSquare's Goulash Newsletter, 22 February 2024, vsquare.org.

Thus, we should assume that it could be serious competition for European brands; currently, the average retail price of an electric car in the EU is about €67,000, while in China it is only €31,000.¹¹

Hungary is currently the world's fourth largest manufacturer of lithium-ion batteries, but it is poised to climb up to second by 2031, with 217.3 GWh of total annual battery capacity (up from 27.5 GWh in 2021) once all the ongoing projects have been finalised. The UK-based Benchmark Mineral Intelligence, which monitors the markets for the raw materials that are critical to e-mobility, has pointed out that 86% of this capacity will come from manufacturers of finished batteries (from Tier 1 of the supply chain), more than in any other country in Europe.¹² According to its forecasts, by the end of this decade the world's total battery capacity will reach 7 TWh, including 4.5 TWh supplied by batteries made in China.

Hungary's alliance with China: not without costs

For many years, the inflow of Chinese capital into Hungary was relatively modest. The upturn in the area of investment is therefore a relatively new development. Although Hungary's political narrative has focused on portraying cooperation with China as an alternative to the West, this is not a viable prospect. The 'opening to the East' is yet to make China an equivalent option to the EU; after all, the impact that the benefits of the single market and access to EU funds have had on the Hungarian economy is many times greater than that of China's loans and investments.

However, it is possible that the implementation of major projects in the e-mobility and 5G sectors will significantly increase the ben-

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efits of cooperation with China. The anti-subsidy proceedings that the European Commission has initiated against China with regard to imports of its electric vehicles are vital for Hungary's position in the international electric car industry. The Portfolio website's sources in Brussels have reported that the proceedings, which were launched on the basis of accusations that the Chinese government has subsidised production, will target the manufacturers of the vehicles as well as the components, which would have significant implications for Chinese-Hungarian cooperation in the field of e-mobility.¹³ This could escalate the trade war between China and the European Union, and prompt the latter to hike its import tariffs on electric cars from China (and possibly their components), which could ultimately make Chinese companies more inclined to locate their factories in the EU. Hungary's much higher political openness compared to other European countries and its existing cooperation with China in the e-mobility sector have made it a natural choice for China to further strengthen its presence in the EU market.

However, Hungary's close cooperation with China has come at a political cost on the international stage. The country's role as an advocate for Chinese interests in the EU (and indirectly in NATO) has exposed it to conflicts and weakened its position in both organisations. It has become embroiled in a serious dispute with the European Commission over its failure to comply with the EU's public procurement rules during the implementation of the Budapest-Belgrade rail link, which was supposed to be the flagship project of the '16+1' format. NATO countries, for their part, are concerned about closer Chinese-Hungarian cooperation under the agreement on 'public security' that the two countries

¹¹ F. Munoz, *EV price gap: a divide in the global automotive industry*, JATO, 2023.

¹² 'Hungary set to be Europe's leading tier 1 battery producer this decade', Benchmark Source, 22 December 2022, source: benchmarkminerals.com.

¹³ D. Szabó, 'Von der Leyen a magyarországi akkumulátorgyárakra is célkeresztet festhetett', Portfolio, 14 September 2023, portfolio.hu.

signed in February this year. From NATO's perspective, another major issue is the cyber security risks arising from Hungary's high level of openness to cooperation with technology companies linked to the Chinese party-state apparatus, such as Huawei. These risks are all the more serious given that Hungarian companies cooperating with this entity on 5G have been strengthening their position in the Western Balkans: for example, Hungary's 4iG is an important player in the telecommunications sector in Montenegro.

China's limited benefits of friendship with Hungary

From China's perspective, the main added value from its relations with Hungary is the promotion of China's initiatives in the EU arena, such as the Belt & Road Initiative and cooperation with China-based technology companies such as Huawei. For China, Hungary is a partner that offers an opportunity to partially mitigate the negative effects of the EU's assertive policy towards it. Hungary's openness has allowed China to build 'European bridgeheads' for two strategic industries: telecommunications and e-mobility. However, China is aware that Hungary has been pursuing a short-term policy, and that the latter's limited influence on the EU agenda will not reverse those processes within the EU that are negative for China, such as the deployment of a de-risking agenda and the development of economic security tools.¹⁴ Some Chinese experts have also warned in off-the-record conversations that China's strong ties with Hungary may further erode the perception of the former within the EU as a result of the Hungarian government's confrontational stance towards the EU's institutions.

Orbán's transactional policy has also helped China to shape its relations with the entire Central & Eastern European region by 'rewarding' Hungary. The day after Latvia and Estonia withdrew from the '16+1' format in 2022,¹⁵ CATL announced the largest-ever foreign investment in Hungary. Although the company insisted that its decision was strictly business-related, in all likelihood it was also a political signal from the Chinese government to the region. After years of disappointment resulting from the Chinese capital's scant involvement in Central & Eastern Europe and the region's growing ties with Taiwan,¹⁶ China has made it clear that maintaining a positive political climate ultimately helps to attract investment from China.

However, China has been frustrated by the delays and low effectiveness of its projects in Hungary, which have prevented Chinese construction companies from building a solid portfolio that would have cemented their credibility and position in infrastructural tenders across the EU. The construction of the Budapest-Belgrade railway link is a case in point. In this instance the Chinese side was irritated by Hungary's protracted dispute with the EU, which led to long delays in implementing the project and was seen by Beijing as a sign of the Hungarian government's incompetence in dealing with 'internal' challenges. During a personal meeting in Beijing on the sidelines of the Belt & Road Forum in November 2023, President Xi Jinping reportedly pressed Orbán to find a solution that would make it possible for Hungary to complete the project together with a Chinese contractor, and urged Hungary not to seek any other partners to finalise it.¹⁷

¹⁴ See P. Uznańska, 'The EU clashes with Beijing: the EU-China summit', OSW, 13 December 2023, osw.waw.pl.

¹⁵ See J. Jakóbowski, J. Hyndle-Hussein, 'Łotwa i Estonia poza formatem 16+1', OSW, 12 August 2022, osw.waw.pl.

¹⁶ See M. Wasiuta, J. Jakóbowski, 'Napięcia czesko-chińskie z Tajwanem w tle', OSW, 9 September 2020; J. Hyndle-Hussein, J. Jakóbowski 'A new phase of China's pressure on Lithuania: weaponisation of European value chains', OSW, 22 December 2021, osw.waw.pl.

¹⁷ 'Orbán travels to Beijing, commits to Chinese rail tech' [in:] S. Panyi, 'Goulash: spying in Brussels, Orbán in China, human trafficking in CEE', VSquare's Goulash Newsletter, 26 October 2023, vsquare.org.