China-CEE Institute
中国—中东欧研究院

December 2022
ISSN: 2560-1628
2022 No. 2

WORKING PAPER

China and Hungary in a disrupted world: China policy in Hungary in 2022

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Kiadó: Kína-KKE Intézet Nonprofit Kft.

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Csaba Moldicz[1]

Abstract

The year of 2022 will be one of historical years to remember for many decades, this year will go down in history as a juncture when initially small differences in policy responses to global pandemic and the war in Ukraine led to different foreign policies and ultimately, they also created divergent paths in history.

Hungary's China policy seems to be one of the most consequent ones in the region, while other Central European countries appear to have changed the course of their China-policy and attempt to get in line with the U.S. foreign policy goals. The best examples of this altered course of foreign policy are Estonia and Latvia, who left the 16+1 cooperation in August 2022 or Lithuania who quit the formation a year before. This paper attempts to characterize Hungarian foreign policy regarding China in two ways: (1) it explains the economic development factors and aspects that strengthen economic cooperation with China (2) and it also contrasts Hungarian foreign policy with Baltic countries' China policy.

The basic research question of the paper is why Hungary can keep the China-friendly course of the foreign policy. By doing so, the paper relies on secondary data and exiting literature. There is special case of investment which is investigated in the paper in details. There are several reasons for that: the investment is the largest ever in the Hungarian economy, the sector of the investment is of special relevance to the long-term development of the Hungarian economy.

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1. Why is Hungary‘s foreign policy unaltered towards China? Economic development factors of Hungary's China-policy

In contrast to the Baltic countries, Hungarian foreign policy has consequently tried to put emphasis on the economic interest of the country in the last decade. With this, Hungary seems to be more successful than Baltic countries that were basically not able to make significant Chinese investments and technology transfer. In the next part we take a case where we try to show the Hungarian management and interpretation of Chinese investment **(1.1. The case of CATL)**, then we also take a look at the broader picture, the principles of foreign policy that guide Hungary's relation to China. **(1.2. The broader perspective of Hungary's China-policy).** In the last part of the chapter, we focus on long term economic factors shaping the relations between China and Hungary. **(1.3. Long-term factors of Chinese and Hungarian relations)**

1.1. The case of CATL

The investment case we take a look at is the investment of the Chinese CATL (Contemporary Amperex Technology Co.) which is one of the largest storage battery producers in the world and decided to invest in Eastern Hungary. According to plans, the company is to invest in a 7.3 billion euros battery plant in Hungary, Europe's largest so far. After receiving the necessary approvals the construction of the 100 Gwh plant will not last more than 64 months. Once the factory is built, it can produce batteries for Mercedes, BMW, and Volkswagen. (Reuters, 2022a August 12). Mercedes has already confirmed the cooperation between the two companies: "With CATL we have a technology-leader as our partner to provide us—as the first and biggest customer of the new plant's initial capacity—with top-notch CO_2 neutral battery cells for our next generation EVs in Europe "—a management board member said. (Reuters, 2022b August 12),

Other more general data also confirm the success of Hungary's opening to the East. (See table 1, table 2 and table 3!) When you look at these tables, it is clear Hungary not only benefited from Chinese investment above the economy's size (relatively) but also in absolute terms as well. In table 1 we can see recent investment data from balance of payments reports of the central bank, while in the second table we see data compiled by the American Enterprise Institute and the third one shows the stock of cumulative Chinese direct investment in the Central European countries.

The data set of the Mercator Institute for China Studies or the China Global Investment Tracker compiled by the American Enterprise Institute uses a different approach to collect data on Chinese FDI in Europe and other regions. Since they trace the investment back to the owner and do not include returns to China, these combined annual values of transactions are usually much higher than the data sets with the BOP approach.

Table 1. Foreign direct investment stock without special vehicle entities (2020)	
	China and Hong Kong
Poland	793 million US$
Czechia	715.2 million US$
Hungary	1.548 million euro
Estonia	112 million euro
Slovenia	128 million euro
Source: Databases of the respective central banks	

Table 2. Chinese direct investment stock in Central Europe (2005-2022)	
Poland	1090 million US$
Czechia	856 million US$
Hungary	3750 million US$
Slovenia	1390 million US$
Slovakia	130 million US$
Source: American Enterprise Institute's China Global Investment Tracker, retrieved from: https://www.aei.org/china-global-investment-tracker/	

Table 3. Chinese cumulative direct investment stock (200-2021)	
Poland	2.4
Czechia	1.3
Slovakia	0.3
Hungary	2.9
Slovenia	1.3
Croatia	0.4
Estonia	0.2
Latvia	0.1
Lithuania	
Source: Kratz, at al. (2022). Chinese FDI in Europe: 2021 Update Investments remain on downward trajectory – Focus on venture capital. Retrieved from: https://merics.org/en/report/chinese-fdi-europe-2021-update	

The interpretation of the CATL investment has been very different in China, Hungary and the West. While the majority of the Hungarian press was positive about the investment, one article in the Portfolió criticized the support of the Hungarian government. (Komócsin, 2022, August 18). The article maintains that the investment is a mistake from the government because in Europe there are plans about how to get rid of "Chinese raw materials and products". The article is not only biased but it also lacks information. China has never been a significant importer of raw materials to the EU. The second argument of the article is also flawed as the author claims that the investment will not lead to technology transfer from China. Obviously neither Suzuki, nor Mercedes, Audi, companies who invested in Hungary, diffuse their technology as the very technology forms the basis of competitive advantage they have over other players in the market. But there are spillover effects in every case, and the 9.000 jobs to be created by the CATL investment in Debrecen too, will be also a significant contribution to the Hungarian economy.

A hint of the Chinese interpretation can be received from the editorial article of the Chinese Global Times, which argued that the investment decision was not the result of excellent political relations between the two countries but the result of a simple business decision: "Why did Hungary attract investment from CATL? Anyone with discerning eyes can tell that this is a perfectly normal business decision. The geographical location in the heart of Europe, with a good industrial support base, allows Chinese companies in Hungary to be closer to their European customers and be able to respond to their needs in a timely manner. More critically, Hungary offers Chinese companies predictability in terms of policy and business environment. Hungary, the first country in Europe to sign Memorandum of Understanding with China on jointly building the "Belt and Road" Initiative, has offered Chinese companies a lot of preferential policies for their investments." (Global Times, August 15, 2022)

This argument can be supported by the fact that the Korean SK Innovation, Korean manufacturer of car parts chose also Hungary for the location of its European electric battery plant last year. Moreover, Hungary seems to be the most preferred location of Asian investors in this sector. In addition to the CATL investment, Asian companies in electric battery business have invested almost 7 billion euros in 17 Hungarian locations. On the other side, the sector seems to be a focal point of long terms strategic interest for Hungarian economy, the Hungarian foreign minister said at the inauguration of the Korean investment: "Whoever wins the electric car investments will win the future, and can lay the foundations for future economic growth" (Szijjártó cited by Hungary Today, 2022, June 17),

The interpretation of the Hungarian government is obviously positive, it sees the link between the investment and the Eastern Opening Policy. State Secretary, Levente Magyar said: "The

Chinese investment is in the field of electric vehicle manufacturing. This also confirms that the government made the right decision when it announced its strategy of opening up to China and identified the electric vehicle industry as one of the main axes of Hungarian economic development." (Magyar cited by Deme, 2022, August 22).

As we could see in this case, there is a link between good political relations and Chinese investment in the given region, but this is also clear that without the promise of profits and good business, the CATL would have never invested in Hungary.

1.2. The broader perspective of Hungary's China-policy

In the former chapter, we have seen that Chinese investment do not take place without the creation of an attractive business environment. At the same time, we can also see that Hungary regards Chinese investment as diversification and not as politics, although in Western media and academic publications, the Hungarian turn towards China is often explained by political motives, and it is frequently framed as the foreign policy of an "illiberal, authoritarian state", but the interpretation is flawed and it can be explained by the next factors:

1. Weak Central European states have undergone a *centralization process* after 2008-2009 to respond the economic and social challenges posed by the Global Financial Crisis in order to tackle the issue of one-sided dependence in terms of capital and technology. Because the economic dependence on the West did not disappear with the reintegration into Western European frameworks, and the asymmetry became even greater in the years following 1990, the Central European tried to take advantage of China's economic rise. The dissatisfaction with the EU membership grew after the Global Financial Crisis and as Thomas Piketty pointed out in 2018, the profits and revenues from property leaving the countries of the Central and Eastern European region represent a much higher number than the EU funds, so the argument that these countries were the clear winners of the EU regional funds is completely wrong (Piketty, 2018). We should add that there is no problem with Western European countries taking advantage of the Central European countries' situation and making money from that, but it shouldn't be a problem that Central European countries fight back.
2. A clear sign of technological lagging is productivity differences between the West and the East in the EU. The gap between productivity and wage developments. Novokmet and

Bukowsky emphasize the gap between productivity and wage development were seen as evidence of asymmetric dependence: “A rise in productivity is the only way to increase living standards in the long run, which is usually translated to the majority of people through higher real wages. However, average wages have lagged behind the productivity growth in CE Europe, or there was a ‘decoupling’ between the potential for rising living standards and the actual rise.” (Novokmet & Bukowski cited by Léotard, 2018, June 11) Because this process mainly attempts to eliminate or at least mitigate the one-sided reliance on the West in the field of economy, first-level opponents, whose requests on home country governments do not go unnoticed, can be found in the business sector.

3. The restructuring process of the Hungarian economy logically goes against the interest of multinational firms here, that originate mainly from Germany, the US, the UK, France, the Netherlands, Belgium and Austria. Because of its past, Germany—the most important one among the above-mentioned ones—avoids open political confrontations with Central European countries—if it is possible—it uses the European Commission as its proxy in these debates.
4. Another layer of this debate comes from the “identity politics" debate which was exported to Europe from America. After the collapse of socialism in Europe, social democrat parties were out of answers, caught in an ideological crisis. After a period of failed experimenting with new ideology—see Gerhard Schöder’s (Germany), Tony Blair’s (UK) and Bill Clinton’s (U.S.) “third way politics”—the solution came from the American left. The original idea was to focus on minorities, specified strata of the society and it turned out to be very successful. Identity politics was originally an answer to growing inequality, social and racial tensions. However, it grew into tribalism and took roots in the far-right too. Politics of Central European conservative governments’ actions and policies are often viewed through the lenses of “identity politics” and criticized this way. This is a total misunderstanding of local (Central European) politics by Western observers, because the reforms and policies of Central European countries are often sweeping social reforms far away from pursuing identity politics.

1.3. Long-term factors of Chinese and Hungarian relations

There are four main factors to influence these relations. (1) The economic rise of China (and East Asia) makes the Hungarian turn to these regions inevitable. Despite critical remarks this is free of ideology and other considerations, it only focuses on the economic needs of the country. (2) The second factor is linked to the first one, Hungarian needs of economic diversification motivate this turn to the East. (3) The third factor comes from politics, which means that sovereignty seems to be equally important to both countries. (4) Hungary is not unique in the fourth factor but the country (along with Serbia) is very consistent in maintaining good political relations with China leading to business opportunities for these countries. Let's discuss these factors in more detail.

- In the long term there is a very **clear shift of economic power** Hungary would like to benefit from. The shift of economic power to the East also opens up new opportunities for Central European countries. Whereas in 1980 the G-7 countries accounted for more than half of global GDP (measured in purchasing power parity [PPP]), today the ratio is less than one-third, while the share of emerging and developing Asia[2] grew from 8.82 percent in 1980 to 33.12 of global GDP in 2022. China is another excellent example, as its share of global GDP (PPP) was 2.26 percent in 1980 and rose to 18.79 percent by 2022. According to the IMF, it will rise to 20.31 by 2027. India has also experienced similar, though somewhat less rapid, growth over the same period. Its share of global GDP was 2.8 percent in 1980 and will be 7.31 percent by 2022.[3] The IMF predicts that the rise of these countries is not over yet; emerging and developing Asian economies will continue their rapid growth and reach 36.67 percent by 2027. Table 4 and 5 summarize the slow, but obvious shift of economic power from the United States to China too.

[2] Based on the classification of IMF: Bangladesh, Bhutan, Brunei Darussalam, Cambodia, China, Fiji, India, Indonesia, Kiribati, Lao P.D.R., Malaysia, Maldives, Marshall Islands, Micronesia, Mongolia, Myanmar, Nauru, Nepal, Palau, Papua New Guinea, Philippines, Samoa, Solomon, Islands, Sri Lanka, Thailand, Timor-Leste, Tonga, Tuvalu, Vanuatu, and Vietnam.

[3] The data are from the database of IMF World Economic Outlook October 2020.

Table 4. Share of global GDP (PPP, %)		
	China	United States
1980	2.26	21.33
2022	18.79	15.78
2027	20.31	14.6
Source: IMF database.		

Table 5. GDP (current prices, billion US$)		
	China	United States
1980	303	2.86 thousand
2022	19.91 thousand	25.35 thousand
2027	29.13 thousand	31.97 thousand
Source: IMF database.		

– Not only is economic power shifting from the United States to China, but China has made significant advances in technology Hungary can benefit from.[4] (See the case of CATL or Huawei investments in Hungary!)

– There is also another reason why economic cooperation with China can be tempting to Hungary. **Nationalism and sovereignty** are more reflected in the foreign policies of China and Central Europe than in Western Europe. While Western European countries seem to have a post-nation development stage which is more friendly to migration, heterogeneous societies, Central Europe and China are more concerned about sovereignty issues and sweeping social reforms than identity politics which debate seems to take a central stage in the political discourse of the West.

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[4] **Patents:** According to the World Intellectual Property Organization (WIPO), China led the world in patent filing with 2.5 million applications. China's performance was two and a half times better than that of the United States. We had the same situation with trademarks, as China registered 9.3 million trademark applications, compared to 900 thousand in the U.S. (World Intellectual Property Organization, 2021).
5G technology: We should add that the improvement in technology indicators can only be partly explained by the sheer size of the market—indicators such as the number of mobile users, science and engineering graduates, and number of publications. But there is another area where Chinese companies have the upper hand in terms of market share and number of patents: That is in 5G. According to the market and consumer data firm Statista, as of October 2021, China had a 41.3 percent share of patent families, while Korea was second with 19.8 percent, and the U.S. was third on the list.
Education: China overtook the United States in the production of science, technology, engineering, and mathematics (STEM) PHDs. China graduated 39,830 students in 2019, while the number of STEM PHDs in the United States was 30,609. According to the Center for Security and Emerging Technology (CSET), this number will increase to nearly 60 thousand in the case of China, while it is expected to be around 35 thousand in the United States. (Zwetsloot et al., 2021 p. 5) Based on future scenarios, Zwetsloot et al. conclude: "Given the scale of Chinese investment in higher education and the technological competition between the United States and China, with much at stake, the gap in STEM doctoral production could undermine the long-term economic and national security of the United States." Zwetsloot et al, 2021 p.10). What is a threat to the United States is a potential opportunity for Central Europe.

– The need for **economic diversification** is palpable in Central European countries, however, Hungary seems to be more successful in its efforts to cooperate with China in the economic sector.

  ○ In the case of Hungary (and even Slovenia Chinese investments were much more significant than in the above cases in terms of GDP. (See table 1!)

Table 1. Chinese FDI as % of GDP, ranking based on the relative size of Chinese FDI to GDP			
	Chinese FDI stock between 2005 and 2020 (billion US$)	GDP (billion US$, 2019)	Chinese FDI as % of GDP (%)
Slovenia	2.18	54	4.04
Hungary	5.88	161	3.65
Czechia	0.96	246	0.39
Poland	2.28	592	0.39
Latvia	0.10	34	0.29
Source: own calculation based on World Bank data and the AEI's China Global Investment Tracker (American Enterprise Institute, 2020)			

  ○ Trade deficit with China increased in all Central European countries but Hungary and Slovakia are the economies where this increase was moderate and at the same time China could grow into a more important trade partner. (The increase in trade deficit was moderate in Latvia, however, the share of China is still very low.) (See table 2.!)

Table 2. Merchandise trade with China in 1999 and 2020 (%)						
	Export share to China (%)		Import share from China (%)		Difference between export and import share	
Year	1999	2020	1999	2020	1999	2019
Hungary	0.28	1.72	2.18	7.95	-0.90	-6.23
Czechia	0.21	1.35	1.96	18.10	-1.75	-16.75
Poland	0.49	1.20	2.66	14.45	-2.17	-13.25
Slovakia	0.06	2.70	1.28	6.74	-1.22	-4.04
Estonia	0.11	1.67	1.17	9.30	-1.06	-7.63
Latvia	0.01	1.17	0.51	4.19	-0.50	-3.02
Slovenia	0.15	0.85	1.34	7.33	-1.19	-6.48
Source: World Bank WITS database						

– The pragmatic Hungarian approach made foreign decision makers aware of the fact that China's economic development policy is more intertwined with its foreign policy than

America’s. It simply means you need very good political relations with China and only this way Chinese companies get “green light” from politics and invest in the country in question, while this link between politics and the business sector is much weaker in the American case.

2. A U-turn in China-policy?

There are other countries in Central Europe who made a U-turn in their China-policies. The Baltic countries, Czechia and Slovakia altered the foreign policy course regarding China in recent years. The first sign was the start of the trade war between the United States and China in 2016 but the real dividing line came with the eruption of the global pandemic and the ensuing deterioration of Sino-American relations. The growing Russian and Chinese cooperation in recent months, or years–vividly expressed in the phrase in “no limits”[5], also had an indirect but clear impact on China-policies of these countries. The improvement of Chinese and Russian relations had a deep and negative impact on the 17+1 cooperation too. Lithuania left the format in 2021, then Latvia and Estonia decided to leave the cooperation in early August 2022 (Lau, 2022, August 11). In the explanation, Estonia referred to the importance of “rules-based international order and values such as human rights.” Zhang Hui cites analysts calling this policy “short-sighted” in his article: “Estonia and Latvia, trapped in the anxiety of geosecurity and under pressure from the US, have withdrawn from cooperation between China and Central and Eastern European Countries (China-CEEC Cooperation), which, Chinese analysts said, is a "shortsighted approach" and means they will lose their diplomatic independence and sacrifice their opportunities for development.” (Hui, 2022, August 13).

For a while, there have been rumors of the cooperation to fall apart or collapse, however, China does not seem to give up the communication and cooperation channel. Zuokui told the media that the move is rather part of framework optimization. (Zuokui interviewed by Hui, 2022. August, 13.)

[5] At the Sino-Russian summit during the Winter Olympics in Beijing (February, 2022), the joint communique of the two countries used this phrase, and its content has been a topics of debate among experts since then.

What we must understand in this context, is that the move of the Baltic countries is not about China or China-CEE cooperation or even its meager result, the step must be interpreted in a broader context. See the similarities of the Baltic foreign policies which we can summarize in four points:

1. Russia is the main threat. The Latvian, Estonian and Lithuanian foreign policy – no surprise – see Russia as the main security challenge for the country. The leaders of the three countries visited Ukraine to show their support and solidarity twice in 2022. The first one was basically just a few hours before the invasion started on February 24, 2022 and the second visit took place in early May, 2022.
2. Russian ethnic minority as a security threat. In these three countries to a varying degree, the Russian minority plays a significant role in society. Different approaches can be found in the literature about whether Russians in these countries can pose a threat or not, however, regardless of the answer, it is always a card which can be played by Russia.
3. Supporters of NATO and EU integration. Baltic countries are very small countries, small countries have different priorities, their existence depends on cooperation with others. The level of economic and political integration determines the possible number of countries in the world. The more successful military alliances and the integration of the world economy are, the more likely it is to form a new entity (country) since the cost of "maintaining" countries and the intensity of security threats become lower. We live in the age of de-globalization and more frequent military conflicts, so these countries subordinate every other foreign policy goal to strengthen economic and military security.
4. China is regarded as a threat. Because this security can only come from NATO and the EU, other aspects of their foreign policies are adjusted to the priorities of the US, and the EU. For this reason, it is no surprise that these countries distanced themselves from China, although China is not really a threat to them.
5. Foreign policy based on values. This policy goes against their economic interests; however, security challenges are more important for them at the moment and therefore they subordinate economic interests to security priorities.

Therefore, we can ask ourselves whether the reference to European values and democracy really reflects the essence of this foreign policy or whether these countries are simply pursuing a rational foreign policy in which security is paramount.

3. Business in foreign policy?

At the same time, the expectations of local elites regarding the volume of FDI from China have not been met. Only Slovenia and Hungary can boast significant Chinese FDI, but even in these cases the amounts fall short of initial expectations. Why? We need to clarify that the motivation for Chinese investment only partially coincides with the conditions that Central European countries can offer. If we use Dunning's classic framework to understand the motivation of Chinese direct investment, we need to look at four factors. Dunning divides the motivation for foreign direct investment into four categories (Dunning, 2000: 163-190):

1. Resource seeking direct investments;
2. Market seeking direct investments;
3. Efficiency seeking direct investments;
4. Strategic asset seeking direct investments.

1. Central European countries are poor when it comes to natural resources. Poland is perhaps the only country where raw materials (copper) play an important role in the export structure. Slovakia, Slovenia and the Baltic countries export wood and wood products to China in a rather insignificant volume. Hungary is the least resource-rich country in the region and offers no natural resources to China. The only resource these countries can practically offer is relatively cheap labor, which is no less abundant in China than in these countries, meaning that the two regions compete rather than complement each other.

2. The markets of the countries are small—only Poland can offer a larger market—but even in this case we should add that the main attraction for China is the Single Market with about 448 million customers. In other words, it is highly unlikely that Chinese companies would target any Central European country, but the entire Single Market.

3. Efficiency seeking investments are typical when the division of labor between subsidiaries can contribute to better and more efficient production at the group level. Exploiting local advantages and combining local strengths or compensating for weaknesses is one reason why multinational companies invest in other countries. Usually, this investment phase prevails when previous investments (market- and resource-oriented investments) can be reorganized, and in this way higher efficiency can be achieved. We have argued above that neither resource-oriented nor market-oriented investments are prevalent in China-CEE relations, so efficiency-oriented investments are not typical either.

4. Among strategic assets, technology, brands and land are worth mentioning. Regarding technology and brands, Western and Scandinavian countries are more attractive to Chinese companies than Central Europe. Although Italy does not score well in innovation, its classic luxury brands are very attractive to Chinese companies, something Central Europe can rarely offer China. Investments aimed at acquiring strategic locations (land, ports, etc.) are typical of Chinese investments in the world, but they are also not typical of the Central European region.

Looking at these four motivations, we can understand why the main targets of Chinese direct investment in Europe not Central European countries are, but Western Europe. Only Hungary performs better than its stage of development and location in Central Europe would suggest. However, the first three major Western European countries (the United Kingdom, Germany and Italy) account for 39 percent of Chinese direct investment in the region. The figures show that the main destinations of Chinese direct investment are large, mature economies, and smaller Western European economies also do well, such as the Netherlands and Finland. Both alone have attracted more Chinese direct investment than the entire Central and Eastern European region.

4. Summary

The article shows the results and main motivations of Hungary's China policy with a strong focus on this year. The war in Ukraine overshadows other geopolitical trends in the world. One of them is the change in China policy of many Central European countries. The main reason for this change is not a change in the course of Chinese foreign policy, but pressure from the United States. The U.S. seems to be engaged in a global struggle with China, which is being fought at all levels and in all regions. Central Europe is one of them. The Baltic countries "pay" for their security with a total alignment with the goals of U.S. foreign policy, which include containing China, while Hungary is not influenced by these games (as it is in a more favorable geopolitical position) and focuses only on its economic interests, in this case economic cooperation with China. The case study we presented was CATL's investment in Hungary. The investment showed well that it fits Hungary's long-term development goals and that there is harmony between foreign policy and foreign trade policy in Hungary.

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