

POLICY Brief

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CHINA AND WESTERN BALKANS

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About

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I. BELT AND ROAD INITIATIVE AND THE 16+1 COOPERATION

I.1. One of the many views from Europe

In Europe there are different perceptions of BRI and of 16+1CI according to whom we ask: media, businessmen, local population, politicians, or scholars. In general BRI is perceived as the major strategic initiative coming from China with a strong mercantile and investment component around principal transport routes that connect China and Europe.

On top of reducing the cost of transport, the BRI economic component tries to respond to over-dependence from capital investment in China, to the goal to make Yuan more a global reserve currency¹, to increase the demand abroad for Chinese goods & services; and to secure the energy supply networks through Asia deep-water ports. At maturity, investment in the Belt and Road is expected to reach \$4 trillion, equivalent to China's 2015 foreign currency reserves².

16+1 Cooperation initiative (16+1CI) adds institutional cooperation to the mercantile feature of BRI. It is multi-sector, focused in a defined geographical space – former COMECON, - and possesses a more coherent governance architecture. Secretariats for each sector have been set in almost every CEEC.

16+1CI gathers a heteroclite assembly of different European countries. Hence, it is very difficult to pinpoint a common

rationale of interest shared by each European country, beyond the aim to attract the maximum of Chinese capital.

It is often argued that Chinese see CEE as an access platform to the bigger and richer Western Europe market, and to its advanced technologies³. This approach requires a precise vision, high capacity of information-gathering and analysis, of planning and coordination amongst Chinese institutions, its banks, and its public and private enterprises endeavoring in CEE. It also requires a faultless implementation capacity, and immense financial power. As we will see further on, the view of the current Chinese investment foray and access in public markets in CEE does not offer this perfect image of a meticulously designed and implemented strategy.

Another feature of the EU-view of BRI is that Europeans see it mostly as between China and Europe. The other countries in-between are considered as intermediate passages and not as Chinese policy targets *per se*. The in-land Chinese and China-close neighborhood role of BRI are not very visible in European explanations and assessment. The fact remains that until now it is China's close neighborhood that has received the bulk of Chinese investment.

¹ A strategic important step has been reached on 13 June 2017 when the ECB invested the equivalent of EUR 500 million in yuan. Incidentally this was the first time that ECB sold USD. www.afp.fr

² *China's belt and road initiative motives, scope, and challenges*, Ed. S. Djankov & S. Miner, PIIE 2016, pp. 8

³ for an original and innovative analysis, see "*Continental drift: Germany & China's inroad in the German Central Eastern European Manufacturing Core*", by Dr. Jacopo Maria Pepe, paper presented at the ISA International Conference, Hong Kong, 15-18 May 2017

I.2. BRI vs. 16+1: between doing business and institutional cooperation

While BRI is viewed mostly as an infrastructure connectivity initiative with a primarily mercantile profile, the 16+1CI expands the business and cooperation opportunities around the BRI based on institutional cooperation. 16+1CI scope includes a large number of sectors such as health, research, culture, youth or even local government cooperation. So all by being EU members or candidate countries, CEE countries are involved in institutional arrangements that do not fall under Brussels remit. Hence while BRI is viewed with interest by EU companies looking for market opportunities or alternative financing, and from EU governments (national or regional) looking for fresh investment sources, the institutional cooperation between China and CEEC is viewed with suspicion by Brussels⁴.

When comparing BRI and 16+1, we can observe some features as described below:

- BRI seems to serve as an *ex-post* umbrella for already existing economic and mercantile joint business deals between EU and Chinese companies, public or private. It also "lends its hat" to the connectivity infrastructure projects in Europe implemented and / or financed by Chinese institutions. The BRI "stamp" seems to provide some prestige for Chinese companies as well as a better ranking needed to mobilize financial support mainly by Chinese regional governments;
- 16+1 gives the impression to be a better-designed top-down institutional approach, having somewhat a clearer vision from its inception. This vision is translated in the supporting & back-

office structures and mechanisms that 16+1 CI has when compared to BRI. Almost every sector has a Secretariat;

- BRI focuses on business and connectivity infrastructure - transport, energy and digital -; while 16+1 is multi-sector and multi-actor.
- The actors involved in BRI are mostly government institutions, regulatory agencies and big businesses. The 16+1CI brings into play larger and more diverse number of actors than BRI, such as communities, non-governmental organizations, academia and citizen. It offers a wider ground for development and cooperation, going beyond big investments and infrastructure projects.

Any relevant business opportunity in CEE countries (where BRI focuses), has important political, social, environmental, etc. implications inside the concerned CEE country (and that falls under 16+1 cooperation mechanisms). This fact is expected to increase the harmony amongst both Chinese initiatives.

II. CHALLENGES OF CHINESE INVOLVEMENT IN THE BALKANS

From the business point of view, compared with many countries situated in-between China and Europe, Balkan countries generally offer: (i) higher political trust to Chinese counterparts; (ii) a better sovereign credit rating; and (iii) safe and decent returns for the money that Chinese bankers may be willing to invest. China weight in foreign trade and in FDI in the Balkans is

⁴ discussion with adviser of high EU Official, made on 11 July 2017 on the margins of Western Balkans Summit of Trieste

growing steadily in absolute terms and in comparison with other foreign partners⁵. Its role as "infrastructure developer" is quite visible in transport and energy sectors⁶.

Chinese investments provide a significant and much needed influx of capital in Western Balkans⁷. But at the time of the writing of this paper, we couldn't find any Western Balkans country that has prepared a strategy of dealing with BRI and / or 16+1 initiative⁸, neither one that has appointed / created any institution in charge.

Regarding a comprehensive picture of the progress of BRI and of 16+1 CI, one can start from their stated "target": the list of 12 measures adopted in Warsaw aiming to "promote friendly cooperation with CEE countries". They encompass a large array of sectors and include objectives in terms of policy-making as well as on governance of the 16+1 CI. But to our knowledge there is no official mechanism of assessment and / or to monitor those goals or to verify the achievements. Hence to measure the progress in each of the 12 measures of 16+1CI, a comprehensive research remains to be carried out.

II.1. the learning curve of public works

The participation of Chinese companies in public infrastructure projects in CEE, has faced many challenges. The most talked-about seem to be the EU procurement rules - applicable in both EU MS and in

candidate countries - which do not allow for direct award of contracts without going through an open tender, even when project financing is Chinese.

Labour regulations, specific technical requirements, environmental standards, obligations to consult local communities, corruption allegations, perception of undermining the market by offering low prices, etc. are also quoted as challenges needed to be dealt with by Chinese companies while investing in public infrastructure in the Balkans.

Given the importance of EU funds, BRI actors and Chinese stakeholders are starting to learn avoiding false impressions of success when negotiating with specific countries. The planning of infrastructure networks, technical design, legal framework, budgetary space, procurement, even the consultation of local communities is based in EU rules - and everything falls within the EU umbrella of regulations. Any deal at the country level that breaches the EU rules, will be challenged in court and will impact the cost and efficiency of the project⁹.

Chinese companies have been learning from their past experience and problems regarding low bidding price, weak awareness of rule of law and poor management (local labour markets, traditions and customs, relations with sub-contractors, reflection of cost-variations, etc.¹⁰.

⁵ CEFTA Investment Report 2017, January 2018

⁶ *ibid.*

⁷ China's Balkans Silk Road: Does it pave or block the way of Western Balkans to the European Union? Magda Stumvoll and Tobias Flessenkemper*, CIFE Policy Paper N°66, February 2018

⁸ the same absence of policy documents applies for the Berlin Process as well for the countries that participate

⁹ the undergoing stoppage of works for Belgrade - Budapest motorway following complaint about the procurement procedure, is an illustration

¹⁰ statement from ZHANG Lihua, Professor, Director of Center for China-EU Relations, Institute of International Relations, Tsinghua University, "16+1 Cooperation" in Synergy with the "Belt Road" Initiative", organized by Chinese Academy of Social Sciences, Beijing 25 June - 1 July 2017

II.2 the narrative and time perspective of Chinese investments

Another challenge that needs to be dealt with by Chinese companies is the public image of Chinese investments regarding their impact on environment, on new jobs generation for locals, and of expected contribution to the partner country.

The long-term view vs. short-term return on investment is a choice that Chinese actors should consider while engaging with their European partners (not only in the Balkans). To our opinion given the very large geographical distance, the relatively low communication intensity, the comparatively new history of collaboration, a low level of mutual knowledge on non-business sectors, and the potential of a virtuous circle amongst two blocs i.e. Europe and China, Chinese should avoid to use an exclusively profit-oriented, short term value-for-money approach while dealing with Europe. Any monetary profit - from both sides - should be placed in a long-term perspective.

II.3. the importance of knowing the local context

To be sustainable any engagement should complement the business rationale of infrastructure investments with the need to better understand the local context where these projects will go through, as well as the "European belonging" of local population.

An example of the complex and multi-layered approach can be illustrated by the nature of feedback that Chinese get from interaction with local population. Given the importance that Chinese companies place

on institutional relations when investing in a country, there is an inherent risk of interpreting good relations that Chinese actors have with local politicians and large businesses, as an indicator of the overall country perception of China. In many cases what the citizen thinks and what the politicians / big business declare are quite different. In that situation Chinese actors may find themselves promoting and supporting projects that while on paper look as having the right institutional and political support and check in all the financial boxes, on the ground they meet with resistance from the local citizen.

By the very nature of infrastructure projects, BRI / 16+1CI requires the cooperation and involvement of large companies. This feature alienates the local SMEs which form the largest number by far of the productive structure in the Balkans¹¹. In the worst case, Chinese engagement may be interpreted as profiting only the certain local oligarchs and not the rest of the country, the local communities, or the simple citizen. While large infrastructure investments may make perfect sense financially and economically, it is crucial to get on board the local population both as potential employees but also as the long-term users and beneficiaries of the outcome of the investment.

Other challenges related to the Chinese participation in large public infrastructure projects include the complexity of project preparation and financing dossier; their timely, qualitative and cost-controlled implementation; the need to take into account their dependence from political cycle of the host country, and the need to

¹¹ as an illustration, in Albania the enterprises employing 1 to 4 employees, constitute 90,5% of the total number of registered enterprises by end of 2016, while those employing more than 50 employees, are 1,05%, at <http://www.instat.gov.al/al/themes/regjistri->

[statistikor-i-ndermarrjeve.aspx](#), "Active enterprises by activity and size", last accessed on 29 August 2017

foresee their post-investment phase (while not relevant for the financial efficiency of the project, it is of utmost importance for the image of BRI in the local population).

III. CHINA AND WESTERN BALKANS: THE CASE OF SERBIA AND ALBANIA

The total trade volume between China and selected Western Balkan economies reached a level of €3.3 billion in 2015-16. In foreign trade, China accounts for almost half of that total trade volume¹².

Regarding the FDI, China is present in all the countries of Western Balkans (except Kosovo): in Montenegro and Macedonia mainly through investment in motorways; in BiH focused in thermal power plants; in Serbia Chinese companies invest in rail, motorways, power plants, metal processing, industrial parks and IT; in Albania in air transport, oil extraction, minerals, etc.

Chinese investment in the Balkans is focused mostly in "fossil industries": energy (coal / gas / oil), transport (autos / airport), and mining / extraction¹³. There is only one investment in telecoms (by Huawei) and one in metal processing (steel production) out of 21 greenfield or merger

/ acquisition from Chinese companies in the Balkans.

Only four Chinese companies (out of which three in Albania) are privately owned; the rest are state - owned companies. This degree of preponderance of publicly-owned companies has been explained by Chinese researchers as motivated by the desire of managers to show back home the profile of a company that is "successful abroad, and especially in European markets". Unfortunately this drive, has not been always followed by proper due-diligence before the investment phase¹⁴.

2009 -2016 China's Investment in the Western Balkans 5¹⁵ (Stock Volume in USD Million)

Country	2009	'10	'11	'12	'13	'14	'15	'16
ALB	435	443	443	443	703	703	695	727
BiH	592	598	601	607	613	613	775	860
MKD	20	20	20	26	209	211	211	210
MNE	32	32	32	32	32	32	32	443
SRB	268	484	505	647	1,854	2,971	4,979	8,268

Source. Huang Ping, Liu Zuokui & al. "The Cooperation between China and CEEC (16+1): 2012-2017, Social Sciences Academic Press (China) 2017

Politically, Chinese officials have publically expressed China's support to the full membership of Western Balkans in the European Union.¹⁶ Lastly, in the 16+1 Budapest Summit in November 2017, financial cooperation between China and Western Balkans got a special mention. All

¹² "The potential for growth through Chinese infrastructure investments in Central and South-Eastern Europe along the "Balkan Silk Road", Jens Bastian, Athens / London July 2017

¹³ see Table 1.2 *China's investment and Construction in the Western Balkans, 2005-16*, in CEFTA Investment Report 2017, by WIIW 2018. We have also counted four investment in Albania that do not figure in the table (airport, oil extraction, copper mine and oil-extraction technology)

¹⁴ Private outbound Chinese investment has soared in 2016 as compared with public one. At the same time private investment in China has dropped sharply. Statement by LV Peng, Researcher, Institute of Sociology, Chinese Academy of Social Sciences

Symposium at the "1+1 Cooperation" in Synergy with the "Belt Road" Initiative", organized by Chinese Academy of Social Sciences, Beijing 25 June - 1 July 2017

¹⁵ Kosovo is not included

¹⁶ H.E. Yu, Jiang, Ambassador of People's Republic of China in Albania, Roundtable on "Albania - China cooperation in the framework of "Belt & Road" and "16+1" Cooperation initiatives", Tirana, October 2017, retrieved December 2017, <http://cdinstitute.eu/web/tryeze-e-rrumbullaket-bashkepunimi-shqiperi-kine-ne-kuader-te-nismave-te-bashkepunimit-brezi-dhe-rruga-dhe-161/?lang=en>

17 parties agreed to *"..explore the possibility of cooperation between CEEC-China financial instruments with the Western Balkans Investment Framework"*.¹⁷ Also under the headline of "Connectivity", *"... participants will further explore synergies between the Belt and Road initiative and the Trans-European Transport Network (TEN-T) and its extension to the Western Balkans"*.¹⁸ Both developments bring BRI and 16+1 closer to the Berlin Process initiative.

III.1. Serbia: importance of public works

Regarding the Balkans data gathered from Chinese researchers indicate a constant increase of the stock volume of Chinese investment. By far the biggest stock as well as the highest rate of increase is in Serbia.

Chinese companies have been active in pan-European corridors going through the Balkans, especially in Serbia. Some of its most important endeavors are:

- *Mihajlo Pupin Bridge* in Belgrade, for EU 170MiO (85% financed by EximBank) implemented by China Road and Bridge Corporation: completed;

- *Corridor X*: (i) *Surcin - Obrenovac*, for 17,6km for USD 103 MiO financed by EximBank: ongoing; (ii) *Obrenovac - Ub*, for 26,2km for USD 301 MiO financed by EximBank, implemented by Shandong Hi-speed Group: ongoing; (iii) *Lajkovac-Ljig* for 24km for USD 301 MiO implemented by Shandong Hi-speed Group: ongoing

- *Corridor XI*: (i) *Central Serbia - Montenegrin Border* (modernization) for 107 km for EUR 106Md to start in 2018 (re-structuring of suburban station in Zemun completed by end of 2017); (ii) *Belgrade - Stara Pazova* (modernization) for USD 319 MiO implemented by CRI-CCCC

- *Belgrade - Budapest railway*, Serbian cost estimated at circa EUR 1Bn for 184km in Serbia (for a total Belgrade - Budapest of circa EUR 3,2Bn) partially financed by EximBank, implemented by China Railway International Company Ltd: started

III.2. Albania: indirect acquisitions and sub-contracting

Chinese support for Albanian economy has been crucial during the 70s and 80s. For example, in 1973 and 1974 Albania sent 24% of its exports to China, from where it received 60% of the total imports. They were mostly in investment goods, which were also financed through financial support from China¹⁹.

The years 1971-1975 were the golden years of China - Albania economic cooperation. There were 132 capital investment initiatives (in all the economy sectors), out of which 75 were completed, 32 in pipeline and 25 ready to start. Major investments such as Fierza HPP, the Metalurgical Combine in Elbasan, Ballsh Refinery, etc have been financed with Chinese money and the technology and the knowhow has been imported from China²⁰.

¹⁷ The Budapest Guidelines for Cooperation between China and Central and Eastern European Countries, 2017/11/28, Art. 6.7, "Financial Cooperation", last retrieved on 6 March 2018 at: http://www.fmprc.gov.cn/mfa_eng/wjdt_665385/2649_665393/t1514534.shtml

¹⁸ *ibid*, art. 4.1, Connectivity

¹⁹ *"Marredhënie Shqiperi - Kine gjate viteve 1960-1978"*, A. Kreka, Tirana University, 2015

²⁰ The bilateral cooperation has been very strong also on the military field. In total Albania received from China in the form of military aid 199 airplanes (70 Mig 17, 12 Mig 19, 12 AN-2, 95 Mig - 19 ES, etc) and 36 helicopters. This is on top of the military aid for the army, and the naval fleet

Lately BRI and 16+1 CI have significantly contributed to the intensification of bilateral China - Albania relations. In 2016 China come third in the volume of exchanges with Albania²¹ (with 7.1% of the total after Italy & Germany), up from the fifth place in 2012. The weight of imports from China has continued to grow over the last five years, reaching 8.8% in 2016 from 6.4% of total imports in 2012. Exports in China have increased by 29.7% from 2012 to 2016 (ALL 5,744 to ALL 7,452), supported by the increase in exports of minerals and oil and of construction materials and metals.

By January 2017, 103 Chinese-owned companies were active in Albania. In stark difference from Serbia, they are all privately-owned. Another interesting difference with Serbia is that, when not sub-contractors of big foreign companies²² Chinese investments in Albania have been carried on through indirect acquisition of shares of Albanian companies property of non-Albanian owners:

- in May 2014, subsidiary of Ekin Maden Ticaret Şirketi Sanayi A.S, a Turkish-based company, sold a 50% stake in Beralb Ltd for \$65 million to Jiangxi Copper Company Ltd. of China²³;
- in September 2016 the Chinese-owned Geo Jade acquired management rights for the largest oil field (operated by Bankers Ltd - a Canadian company) in Albania for USD 575 million;
- in October 2016 China Everbright Limited acquired 100% of the shares of the Tirana International Airport for 30

years, from its German owner.

In 2014 Bank of Albania has concluded a SWAP agreements with Bank of China, which is an important step in supporting bilateral economic exchanges. In April 2017 the Deputy Prime Minister Zhang Gaoli visited Albania where he was received by PM Rama. In May, Chinese government agreed to support the renovation of the Opera House in Tirana with a grant of USD 2 MiO.

Until February 2018, no public works contract seems to have been awarded to any Chinese contractor in Albania. Both Rruga e Arbrit Motorway and Spitala Industrial Park procedures have not gone through.

IV. CONCLUSIONS: AIMING FOR A WIN-WIN-WIN

From the Balkans, the rise of China and its increasing presence in Europe is still in need of a better understanding. Not unlike their EU colleagues of Europe, Balkans' politicians are courting Chinese decision makers - politicians, big companies and banks - mostly for their financial power. In a slow growth / high public debt environment, Chinese foreign direct investment is very welcome.

Chinese actors are aware of their economic and financial attractiveness, as well as of the unease caused by their foray into the European business and larger economic and institutional cooperation scene.

²¹ following data came from "Foreign Trade 2012-2016", INSTAT 2017

²² Huawei, sub-contractor for Albtelecom - a 100% Turkish owned telecom company; and Hilong, sub-contractor in oil-extraction working for SHELL Oil exploration

²³ 2014 Minerals Yearbook, Albania (Advance Release), US Department of the Interior, US Geological Survey June 2016

The immediate conclusions point towards the need for a better communication from both sides, based on nourished debate and increased communication with each other, involving all the stakeholders and not only the politicians, the international finance or the big businesses.

The Balkans need to better grasp the rationale of BRI and of 16+1CI. We need to be able to accept also the possibility that even if it looks as a top down carefully planned endeavor, BRI and 16+1CI may both be still in the phase of design. Chinese partners are realizing that Balkan countries, even if non-EU members, are *de facto* applying the policy-making methodology and the legal framework of the European Union. Their economies are a satellite of the

EU economic power, and follow closely EU economic cycle.

The Berlin process offers an outcome-oriented platform of cooperation amongst EU, Western Balkans and Chinese partners. While Connectivity Agenda invites for cooperation with BRI, the 16+1 Cooperation initiative provides almost the mirror image of the Regional Cooperation component under the Berlin process²⁴.

Given the steady progress of Chinese investment in the Balkans, it must be possible to engage in a constructive way by looking for a win-win-win situation satisfying the Balkan countries, the EU and Chinese partners.

²⁴ for a comprehensive analysis on the Berlin Process, see up-coming paper "Berlin Process: 2014-2018", CDI to be published in March 2018

Annex 1. Coordinating Mechanisms / Platforms of Cooperation of 16+1 CI: March 2018

No.	Coordination Mechanism or Platform	Site of Secretariat	Organizer / Host	Progress
1	China-CEEC Tourism Coordination Center	Hungary	Hungary National Tourism Agency	Set up
2	China-CEEC Consortium Institute of Higher Education	Rotating Presidency	Ministry of Education of each country	Set up
3	Contact Mechanism for the Investment Promotion Agencies of China-CEEC	Poland	Polish Information and Foreign Investment Agency	Set up
4	China-CEEC Joint Chamber of Commerce	Poland-Executive Agency China-Secretariat	China Council for the Promotion of International Trade	Set up
5	China-CEEC Association of Governors of Provinces & Regions	The Czech Republic	Ministry of Internal Affairs of Czech	Set up
6	China-CEE Association for Promotion of Agricultural Cooperation	Bulgaria	The Ministries of Agriculture and Food of Bulgaria	Set up
7	China-CEEC Technology Transfer Center	Slovakia	Slovak Center of Scientific and Technical Information	Set up
8	China-CEEC Think Tanks Network	China	Chinese Academy of Social Sciences	Set up
9	China-CEEC Association on Transport & Infrastructure Cooperation	Serbia	Ministry of Trade and Communications of Serbia	Set up
10	China-CEEC Association for Logistics Cooperation	Latvia	Ministry of Transport & Communications of Latvia	Set up
11	China-CEEC Association on Forestry Cooperation	Slovenia	Ministry of Agriculture of Slovenia	Set up
12	China-CEEC Association on the Promotion of Health Cooperation	China	National Health and Planning Commission	Set up
13	Association for Arts Cooperation	To be determined	To be determined	In progress
14	Association for Customs Cooperation	To be determined	To be determined	In progress
15	China-CEEC Center for Dialogue and Cooperation on Energy Projects	Romania	To be confirmed	To be set up
16	China-CEEC Maritime Secretariat	Poland	Ministry of Maritime Economy and Inland Navigation Poland	Set up
17	China-CEEC Cultural Cooperation Coordination Center	Macedonia	To be confirmed	To be set up
18	China-CEEC Association of Small and Medium Enterprises	Croatia	To be confirmed	To be set up
19	China-CEEC Inter-Bank Association	China-Secretariat Hungary-Coordination Center	China Development Bank, Hungarian Development Bank	Set up
20	China-CEEC Veterinary Science Cooperation Center	Bosnia and Herzegovina	To be continued	To be set up
21	China-CEEC Environmental Protection Association	Montenegro	To be continued	To be set up

Source. Huang Ping, Liu Zuokui & al. "The Cooperation between China and CEEC (16+1): 2012-2017, and CDI own research