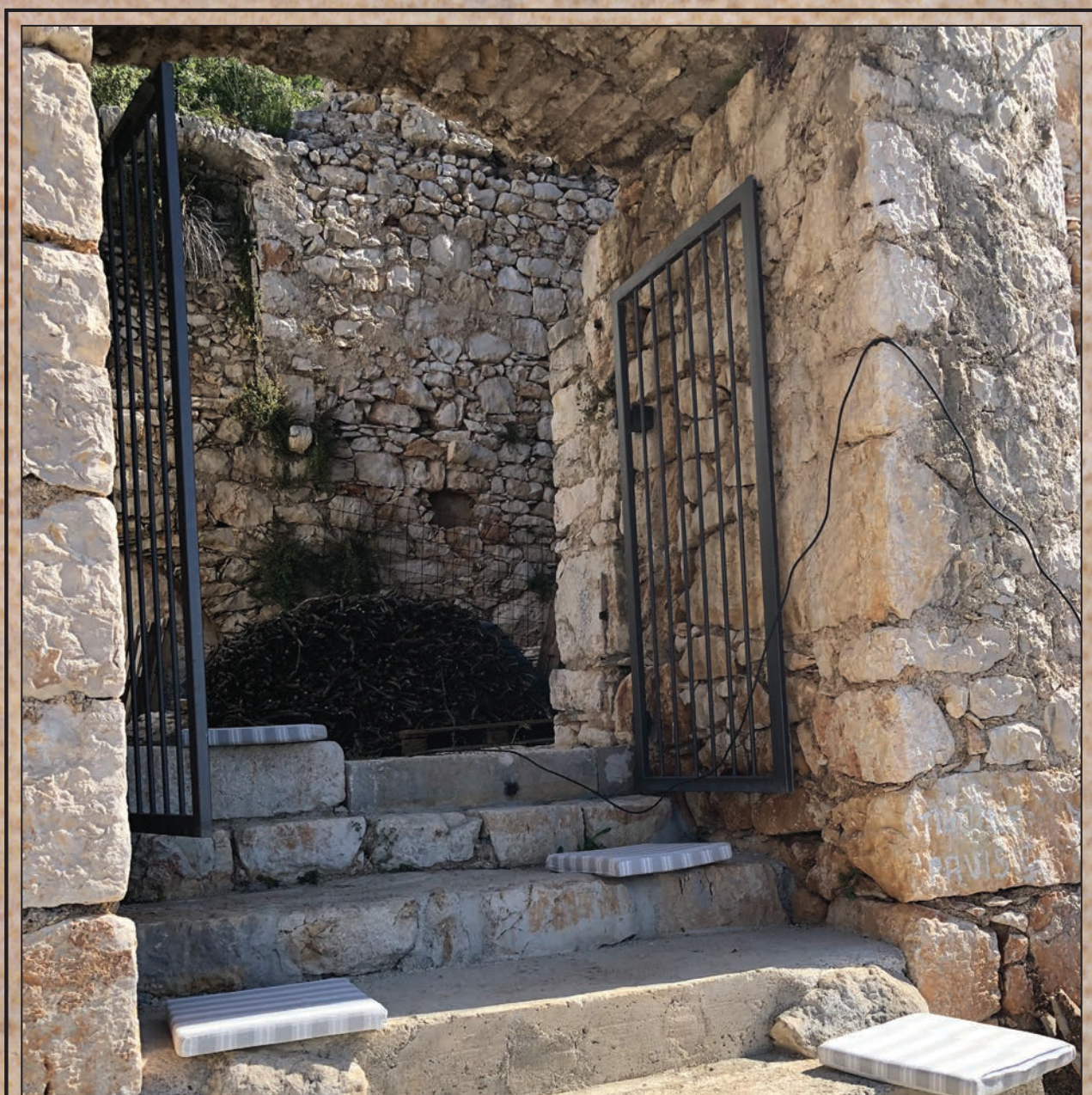


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RETHINKING DEBT-TRAP DIPLOMACY: A CASE STUDY OF MONTENEGRO'S DEBT TO CHINA

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ABSTRACT

This paper analyses the claim that Montenegro is a country towards which China is practising debt diplomacy. The study aims to assess whether Montenegro's borrowing from Chinese banks can be taken as an example of deliberate Chinese lending intended to subjugate Montenegro both economically and politically. The case study method is used to draw conclusions regarding the validity of accusations about the harmfulness of the debt to Montenegro, or lack thereof. In addition, the paper examines the economic parameters of the relationship between China and Montenegro, as well as the political reactions to the indebtedness within Montenegro. It also considers the reactions of the European Union and the USA, within the context of China's geopolitical role in Europe. Based on the findings, it appears unlikely that China is engaged in ongoing debt diplomacy with Montenegro. The criticisms of China's involvement in the Montenegro case seem politically motivated and unwarranted.

Keywords: China, Montenegro, debt-trap diplomacy, soft power

RIPENSARE LA DIPLOMAZIA DELLA TRAPPOLA DEL DEBITO: UNO STUDIO DI CASO SUL DEBITO DEL MONTENEGRO NEI CONFRONTI DELLA CINA

SINTESI

Il presente articolo analizza l'affermazione secondo cui il Montenegro è un paese verso il quale la Cina sta praticando la diplomazia del debito. L'obiettivo della nostra analisi è determinare se i prestiti concessi dal sistema bancario cinese al Montenegro possano essere considerati come un esempio di una deliberata azione di indebitamento finalizzata a sottomettere il paese, sia dal punto di vista economico che politico. Al fine di valutare l'accusa della dannosità del debito nei confronti del Montenegro, è stato adottato il metodo dello studio di caso. Inoltre, l'articolo analizza i parametri economici del rapporto tra Cina e Montenegro, nonché le reazioni politiche all'indebitamento del Montenegro e le reazioni dell'Unione Europea e degli Stati Uniti, nel contesto del ruolo geopolitico della Cina in Europa. Sulla base dei risultati, sembra probabile che la Cina non sia impegnata nella continuazione della diplomazia del debito nei confronti del Montenegro e che le critiche al coinvolgimento della Cina nel caso del Montenegro siano politicamente motivate e ingiustificate.

Parole chiave: Cina, Montenegro, diplomazia del debito, soft power

INTRODUCTION AND THE RESEARCH PROBLEM

This article aims to analyse the claims concerning Chinese debt diplomacy,¹ focusing on the case of Montenegro. In other words, it seeks to assess the relevance of the “China-seizing-assets story” (Deron et al., 2021) in relation to Montenegro. Problematising the indebtedness of Montenegro to China resulting from infrastructure activities initiated by Montenegrin authorities in 2014 introduces a novel aspect to the political landscape. Only in recent years has Montenegro started to be portrayed as yet another example of Chinese debt diplomacy, which allegedly financially enslaves smaller nations along the so-called New Silk Road.

There are several reasons why the case of Montenegro, in particular, needs to be considered from the point of view of problematising debt diplomacy. First of all, it is a very small country, the smallest among those whose borrowing from China is considered problematic.² Soyaltin-Colella (2023) considered the indebtedness of the Montenegrin authorities to Chinese banks as an additional incentive to perpetuate corruption in Montenegro. Bakalov categorically labelled Montenegrin indebtedness as an example of China's debt-trap diplomacy. He even went a step further, suggesting that there is a real danger in the medium and long term that Beijing will have enough economic influence to undermine NATO's capabilities, if not directly, then certainly diplomatically through its economic levers via Montenegro as a member of NATO (Bakalov, 2021, 42). However, Montenegro's geopolitical importance³ far outweighs its size, as it has a deepwater port, which is still majority state-owned and is close to being directly connected to Central Europe via Belgrade and Budapest. In addition, Montenegro is integrated into the Western European and Atlantic security architecture, having been a member of NATO since 2017 and a candidate for EU membership since 2010. Therefore, it is also important to examine how Montenegro's Western partners reacted to the debt issue that arose following extensive borrowing from China.

Debt-trap diplomacy represents a novel phenomenon in political science and diplomatic theory and practice. Unlike classical phenomena in diplomacy,

which, in various forms, have shown continuity over several centuries and even millennia, debt-trap diplomacy is a distinctly modern phenomenon closely related to the diplomacy and economies of the 20th and 21st centuries. For example, commercial diplomacy after the First World War manifested itself through the credit diplomacy of Western creditors and assistance in the post-war reconstruction of Europe (Udovič, 2022). Furthermore, dollar diplomacy has, up to the present day, manifested itself partly through debt diplomacy, especially during the period of the presidencies of William Howard Taft and Theodore Roosevelt. The Monroe Doctrine, which guided US foreign policy during the interwar period, argued for the use of economic means in foreign policy, specifically the granting of loans to the countries of the American continent so that other, non-American countries would not do the same.⁴ Issues of debt diplomacy also arose during World War II, so a broader interpretation of the concept of debt diplomacy could equally be transferred to the American-Soviet Lend and Lease agreement. Finally, debt diplomacy is evident in the case of socialist and federal Yugoslavia, of which Montenegro was a constituent republic from 1945 until 1991; here, the policy of choosing creditors for its dysfunctional economy resulted in the understanding that there was no free lunch when those loans came due (Dyker, 2011).

The authors who have addressed the concept of debt diplomacy agree that the term first appeared in 2017. Since then, the use of the term has spread globally, often accompanied by negative connotations, apparently because of its frequent association with the word “trap”. The influential Indian geostrategist, economist and professor Brahma Chellaney introduced the term “debt diplomacy” in his influential article titled “China's Debt-Trap Diplomacy” (Chellaney, 2017) published in Project Syndicate. In this article, Chellaney uses the term “debt diplomacy” to describe China's low-interest loans to countries around the world as predatory. He contends that China's original intention was to make these loans *de facto* unpayable, thereby gaining influence and power over the indebted countries and forcing them to cede valuable infrastructure to China. According

1 More on Chinese commercial diplomacy cf. Fister & Brglez (2021).

2 Some authors unequivocally consider Montenegro a target of Chinese debt diplomacy (cf. Soyaltin-Colella, 2023; Bakalov, 2021). However, this topic has always been dealt with in a much louder fashion by the media – cf. Schmitz (2021) interviewing, among others, Milica Kovačević, the director of the influential Montenegrin NGO Center for Democratic Transition. Kovačević (2021) is the most comprehensive study on the Chinese loan to date.

3 The Port of Bar is financially and geopolitically the most valuable asset of Montenegro. The port is still majority-owned by the state capital. In 2022, the port's annual transshipment exceeded two million tons, and the total revenue for the same year was over 20 million euros (for more detailed business information cf. the Company Wall electronic register entry at: <https://www.companywall.me/firma/luka-bar/MMTpu2C>). Former Montenegrin President Filip Vujanović emphasized the importance of the port at the Cooperation Forum between China and Central and Southeastern Europe in Ningbo in 2019. He suggested that the Port of Bar could serve as China's port corridor on the Adriatic. The Digital Forensic Center, a prominent NGO from Montenegro, produced a special report in 2023 on the strategic importance of the Port of Bar. This report, titled “Port of Bar - strategic or commercial interest?” discusses why it would be in China's interest to own the port to enhance its maritime influence in the Balkans).

4 For further reading on dollar diplomacy cf. Veaser (2002); Carroll & Herring (1995); Rosenberg (2003).

to Chellaney, China pursued geostrategic dominance by offering loans to other countries for infrastructure development, aiming to “facilitate (Chinese) access to natural resources or to open the market for low-cost and shoddy Chinese goods” (Chellaney, 2017). Chellaney sees the realisation of China’s, a priori negative, intentions through its One Belt One Road (OBOR) initiative which, at the time of the article, was worth over one trillion US dollars (Chellaney, 2017).

The goal of China’s global expansion through the New Silk Road is to foster deeper ties between Europe and Asia (Urban, 2016). The OBOR initiative connects China and Europe through both the sea route and the overland Silk Road. It is envisaged that the direct land route to Western Europe will traverse Eastern Europe, while the sea route to EU countries will pass through the Adriatic Sea (Gruebler, 2021). In order to achieve political and economic connection with the countries of Central and Eastern Europe, the “16+1” initiative was launched in 2012. The cooperation programme for Central and Eastern Europe is comprised of various European Union (EU) Member States in Central and Eastern Europe, including all the countries that joined the EU in 2004 or later (excluding Cyprus and Malta), as well as five Western Balkan countries, including Montenegro, located on the shores of the Adriatic Sea; the “+1” refers to China (Gruebler, 2021). Greece joined in 2019, while Lithuania left the group in 2021 (Lau, 2021) and Estonia and Latvia followed suit the following year (BNS, 2022). Montenegro remains a participant in this initiative, which can be analysed as a quasi-institutional framework for China’s relations with Central and Eastern Europe.

After 2017, a series of analyses, articles, policy papers, and other works dealing with the topic of debt-trap diplomacy appeared within academic and other communities. Following this surge, two researchers from the Harvard Kennedy School published a student paper in 2018 on the new Chinese economic strategy and the challenges it posed for the policy of the United States, using the term “debtbook diplomacy” to describe the same phenomenon that Chellaney had called debt-trap diplomacy (Parker & Chefitz, 2018). The claim that China is deliberately trying to “trap” the countries on its New Silk Road (OBOR) in debt, to increase its geostrategic influence either through the settlement of outstanding debt through the acquisition of valuable ports, transport infrastructure, or mineral resources, or else to achieve political control over these countries, has caused considerable worry at the highest echelons of the political authorities in both the USA and Western Europe. A prominent researcher in Chinese diplomacy, Deborah Brautigam, described the speed and ease with which the new idea-image of Chinese debt diplomacy spread in the US and Western Europe as “The rise of a

meme” in her influential article on debt-trap diplomacy (Brautigam, 2020). Moreover, Google Trends statistics indicate a growing interest in the term debt-trap diplomacy, peaking at a value of 100 in May 2022. However, Chinese politicians, most notably Xi Jinping, contend that no real geopolitical significance is attached to the OBOR initiative (Saich, 2017).

The construction of the narrative about predatory borrowing practised by China was significantly bolstered by the public letter sent in 2018 by Edwin M. Truman, a former Assistant Secretary of the US Treasury at the International Monetary Fund, together with 15 senators, to the US Secretary of State for the Treasury. In this letter, we find a description of how “Beijing’s attempt to weaponize its capital is not just limited to Asia and Africa but extends to Europe” (Truman, 2018). Here, “[t]he term ‘weaponize’ clearly situated China’s lending as an insidious tool, and the letter possessed a series of striking questions about China’s intentions” (Lai et al., 2020, 111).

In 2021, Chellaney once again highlighted China’s debt diplomacy, describing the entire process. First of all, he argues that China does not assess the financial viability of the debtor; instead, it is happy to lend regardless. He then asserts that: “[t]he heavier the debt burden on the borrower, the greater China’s leverage becomes” (Chellaney, 2021). Referring to AidData’s dataset analysis of 100 cases of Chinese loans (Gelpert et al. 2021), Chellaney also notes that:

these agreements arm China with considerable leverage by incorporating provisions that go beyond standard international lending contracts. Such is the lopsided nature of the Chinese-dictated contracts that, while curtailing the options of the borrowing nations, they give China’s state-owned banks untrammelled discretion over any borrower, including the power to scrap loans or even demand full repayment ahead of schedule.⁵ (Chellaney, 2021)

It is extremely important, according to Chellaney, that China obliges the creditor country to maintain confidentiality regarding all the lending conditions. Referring to the aforementioned study (Gelpert et al., 2021), he also says that:

contracts [...] obligate the borrower to exclude the Chinese debt from any multilateral restructuring process [...] This is aimed at ensuring that the borrowing country remains dependent on Beijing, including for any debt relief in the event of financial distress [...]. [...] Infrastructure financing

⁵ This primarily refers to the fact that over 90 per cent of the Chinese contracts they analysed, encompassing all Certificates of Bank Deposit (CDB) contracts, contain provisions that grant the creditor the authority to terminate the contract and request immediate repayment in the event of substantial alterations in the laws or policies of either the debtor or creditor nation.

comes mainly in the form of market-rate loans like those from private capital markets. The more dire the borrower's financial situation, the higher the interest rate China is likely to charge for lending money. (Chellaney, 2021)

What the study does not show is how, in cases of loan default, China charges the indebted countries by taking their infrastructure. Chellaney provides several examples of this form of settlement in his work, including loans to Pakistan, Sri Lanka, and Tajikistan. However, these examples have been analysed in detail elsewhere and dismissed as not being true examples of debt diplomacy (Hwang et al., 2016; Brautigam, 2020; Carmody, 2020; Singh, 2020).⁶ However, once the narrative of the debt-trap diplomacy had been built, it could only spread to other geographical areas where China appeared as a creditor. Although Africa and Asia are not the only continents where China's controversial debt diplomacy has expanded, it is interesting to note that much less attention has been paid in the academic debate to European countries that have accepted loans from Chinese banks.

In this paper, our focus is on Montenegro, a small Mediterranean country which has been in the spotlight of both research and policy communities for several years as another example of China's debt diplomacy. It was only after 2020 that researchers began to discuss several cases of indebtedness among European countries, prominently featuring instances such as the Greek and Croatian ports as well as the indebtedness of Montenegro for the construction of a highway. This highway aims to connect the Montenegrin port on the Adriatic Sea, the Port of Bar, with Central Europe, via Serbia and other countries where road infrastructure is already under extensive construction with financing from Chinese loans. Montenegro borrowed from China in 2014 to undertake the construction of the first highway in its history, with the loan taken from Chinese banks amounting to just over \$900 million. Montenegro's debt to its Chinese creditors, due to the highway, accounts for a quarter of the country's GDP, posing a threat to the stability of public finances if it continues to grow (Grgić, 2017). The construction of the Montenegro highway, funded by Chinese loans, is part of the EU-China Connectivity Platform scheme in Europe (2016–19) (Gruebler, 2021). The list of the projects supported indicates the intention to connect the EU and China infrastructurally to a degree that aligns with the conceptualisation of a New Silk Road.

If we reconsider that the new maritime Silk Road passes through the Adriatic Sea, it becomes evident why, at least hypothetically, Chinese loans, the New Silk Road, and a heavily indebted Montenegro, which is part

of the initiative "16+1", can be brought together into one single geopolitical problem. Therefore, the main research question of our work is set as follows: Is there any justification for the apprehension about Chinese debt diplomacy towards Montenegro?

The analysis of China's alleged debt diplomacy towards Montenegro will be carried out by addressing two further research questions:

1. How does the criticism of borrowing relate to the broader issues of debt sustainability, financial stability, and sovereignty of Montenegro?
2. To what extent does the borrowing affect relations between the European Union and Montenegro, bearing in mind the latter's integration process into the EU?

In this paper, we use the case study method to address the research questions by analysing primary and secondary sources and synthesising the empirical data obtained. The primary sources include statements from political officials, as well as statistical data on Montenegrin-Chinese economic ties obtained from the Chamber of Commerce of Montenegro, the Central Bank of Montenegro, and the Ministry of Finance of Montenegro. The secondary sources are derived from existing analyses of Montenegrin-Chinese economic ties and, specifically, the indebtedness of Montenegro to Chinese banks. These analyses were conducted by both academic and non-governmental organisations.

The paper consists of four sections. The first chapter provides an overview followed by an analysis of the economic and trade relations between Montenegro and China, with a specific focus on Chinese investments in Montenegro. This section aims to present the significance of China's investments for Montenegro and vice versa. In the second section, the paper examines the economic and political aspects central to its theme – Montenegro's indebtedness to Chinese banks for the construction of its first highway. In addition to the analysis of the loan agreement, an overview of the importance of the planned highway in the context of the New Silk Road initiative is also offered. The third section is dedicated to the presentation and analysis of the political reactions of the relevant political actors in Montenegro to the debt, including officials of the Montenegrin government in power until 2020 and those in power after 2020, when the first democratic change of government in this country took place. Additionally, the reactions of the European Union and the United States of America to Montenegrin indebtedness are also analysed, especially in relation to the hedging arrangement that Montenegro pursued with the help of American and French banks after the European Union's refusal to help Montenegro. The final

⁶ Regarding Africa, Deborah Brautigam refers to the largest database of loans that China has given to African countries (Johns Hopkins School of Advanced International Studies), which includes over 1000 such cases. She states that in Africa, there are no instances where it could be said that the Chinese deliberately ensnared another country in debt and then used that debt to extract unfair or strategic advantages, including 'asset seizures' (Brautigam, 2020, 6).

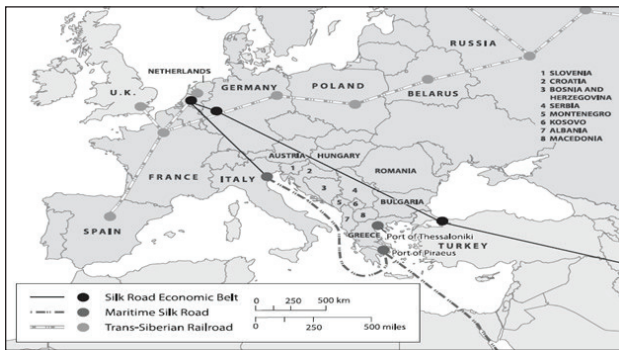


Figure 1: New Silk Road Map with the Balkans (Grgić, 2017, 5).

part of the paper synthesises conclusions drawn from preceding sections in order to answer the research questions.

THE RELEVANCE OF ECONOMIC RELATIONS BETWEEN CHINA AND MONTENEGRO

China's increasing influence in the Western Balkans has been observed since the introduction of the New Silk Road initiated by Xi Jinping in 2013. Two important corridors, namely the Economic Silk Road and the Maritime Silk Road, have been designed to reach the heartland of Europe through Greece via the Balkan Peninsula by connecting land and sea. This form of cooperation at the political level aims to speed up the economic rapprochement between China and the countries of Central and Eastern Europe (hereinafter CEE) (Zuokui, 2014). Figure 1 shows the countries that are directly or indirectly included in the New Silk Road, formulated through the OBOR initiative. It is observed that of the Western Balkans countries, only Serbia is on the trajectory of the Economic Silk Road, while Montenegro, Albania, Bosnia and Herzegovina, and Croatia are on the route of the Maritime Silk Road.

Since 2012, through the OBOR initiative, China has established an institutional framework for future infrastructure projects with significant financing from the state-owned EXIM Bank. Western analysts perceive a geostrategic approach which involves gaining entry to the EU through unconventional means. For China, this presents yet another business prospect, particularly in the energy and infrastructure industries, where its state-owned enterprises have discovered profitable opportunities. Countries that are still outside the EU may provide government assurances for large-scale infrastructure projects, but EU regulations are stringent and impose comparatively rigorous restrictions on non-EU financial inflow. However, on the "European periphery" foreign banks and firms have greater confidence in investing in projects backed by robust state guarantees, which helps mitigate risk (Grgić, 2017, 5).

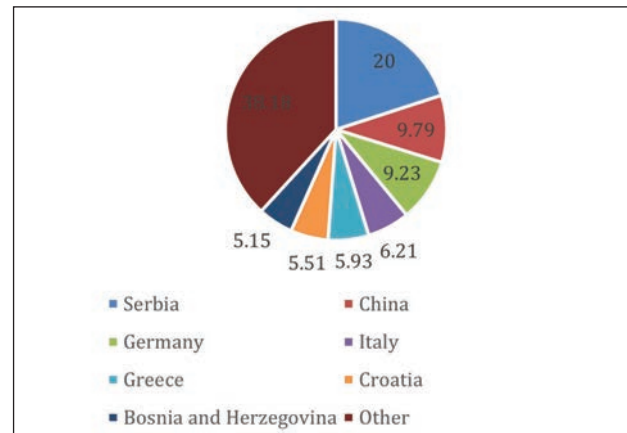


Chart 1: Montenegro imports by country, 2021 (in %)
(Source: Central Bank of Montenegro, 2021a).

In the context of the "European periphery", Montenegro found itself in a political and economic vacuum regarding the construction and financing of the "project of the century" – part of the Bar-Boljare highway. On the other hand, officials in Montenegro did not speak publicly about Montenegro's place in the OBOR initiative, nor did they associate the construction of the highway with this initiative. Such connections were mostly found in the media and partly in the work of some analysts. The Montenegrin authorities overwhelmingly talked about this project as a domestic issue of strategic significance.

There are three important aspects to the economic ties between Montenegro and China over the past 15 years. The first aspect is trade, where Montenegro has been in deficit since 2006. This is understandable, considering its population of only around 620,000 and an economy based on the service sector, particularly tourism. The second aspect involves Montenegro's borrowing of funds from Chinese creditors. The third aspect of these economic relations is foreign direct investment from China into Montenegro.

An essential economic indicator is the direct connection between the two countries through the relationship between exports and imports. Montenegro's main foreign trade partners in 2021 were the countries of the Central European Free Trade Agreement (CEFTA), where 43.21% of goods were exported, the largest proportion of which was electricity. This was followed by EU countries with a share of 31.14%, where the main exports were aluminium and electricity, and the member countries of the European Free Trade Association (EFTA) with 11.6%. On the other hand, the largest proportion of goods were imported from the EU (45.68%), CEFTA and EFTA countries (28.48% and 2.34%), while 23.5% were imported from other countries (Central Bank of Montenegro, 2021a, 117–118). Individually, the largest export partners were Serbia, Switzerland, and Bosnia and Herzegovina. Chart 1 presents the most important

Table 1: Comparison of selected variables in a cross-temporal perspective (Source: the authors).

Structure of Montenegro's external debt as of September 30, 2022		
Creditor	Debt balance (in millions of euros)	Share of external debt (%)
International Bank for Reconstruction and Development (IBRD)	186.94	5.16
Member countries of the Paris Club of Creditors	57.25	1.58
International Development Association (IDA)	14.77	0.41
European Investment Bank (EIB) 1.68 2.40	95.90	2.65
EBRD	58.95	1.63
Council of Europe Development Bank	76.40	2.11
European Commission	60.00	1.66
Credit Bank for Reconstruction - Germany (KfW)	343.54	1.20
Hungarian credit	0.30	0.01
Polish credit	3.10	0.09
French credit - Natixis	0.85	0.02
China EXIM Bank	710.27	19.60
Spanish loan for landfill construction	1.36	0.04
EUROBOND	1,750.00	48.28
IFAD	2.99	0.08
Export Development Canada (EDC)	7.42	0.20
Syndicated loan - PBG	225.71	6.23
Syndicated loan – PBG 2	234.54	6.47
HAPOALIM - Armoured vehicles	14.78	0.41
Rapid Financing Instrument - IMF	79.43	2.19

import partners of Montenegro. In terms of imports, Serbia again holds the first position, followed by China and Germany. China as an export partner does not appear individually in the calculations of the Central Bank of Montenegro due to its insignificant share. On the other hand, China is the second most important partner for Montenegro when it comes to imports. This speaks of the significant dependence of Montenegro on the import of Chinese goods, with China's share at almost 10% (245 million US dollars) of Montenegro's total imports, while the share of China's exports to Montenegro in the total exports of China is negligible (245 million against 3.3 trillion US dollars) (Workman, 2021).

Public debt is a crucial factor in analysing the economic relationship between China and Montenegro. As a country in transition, Montenegro struggles with its level of public debt. The EXIM Bank loan had a significant impact on the growth of public debt, which reached 103% of GDP in 2020. Table 1 presents the latest available data on Montenegro's public debt by lender and the share of individual debt in total public debt. Notably, the debt to the EXIM Bank

constitutes a substantial 19.6% of the total public debt. However, the table also shows that the rest of Montenegro's public debt is owed to banks and international organisations from Western countries. Thus, almost half of Montenegro's public debt arises from the placement of bonds (EUROBOND), while the debt to international financial institutions and banks stands at 32%. As the data show, China is the largest single lender; however, Montenegro exhibits a stronger orientation towards the Western financial market in terms of its sources of financing.

An overview of Chinese Foreign Direct Investment (FDI) in Montenegro indicates its relatively modest volume in the period since the restoration of Montenegrin independence in 2006. Table 2 shows that the amount of FDI in the period up to 2019 was only around 10 million euros. Also, the share of FDI from China in the total FDI averaged 0.129%, or concerning GDP, only 0.027% on average until 2020. The situation changed drastically in 2020, when FDI amounted to 71.2 million euros, making China the largest investor in that year and

Table 2: FDI from China 2006–2020.

Amount of Chinese FDI from 2006 to 2020 expressed in euros		Share of the Chinese FDI in total FDI %	Share of the Chinese FDI in GDP %
Year	Amount of FDI		
2006	219,900		0.01
2007	377,050	0.042	0.013
2008	696,660	0.084	0.023
2009	2,470,800	0.256	0.083
2010	1,694,370	0.305	0.057
2011	840,470	0.185	0.026
2012	440,000	0.084	0.014
2013	141,000	0.035	0.004
2014	1,017,590	0.028	0.029
2015	1,376,240	0.205	0.038
2016	441,000	0.069	0.011
2017	676,730	0.126	0.016
2020	71,234,140	13.9	1.702
2021	6,438,390	0.843	0.13
2022	882,160	0.084	0.015
Total	88,946,500		

the second largest investor in Montenegro in the period from 2006 to 2020, just behind Russia.

In the analysis of FDI in Montenegro from 2006 to 2015, China did not rank among the top 16 countries with the largest share (Chamber of Commerce of Montenegro, 2016). This can be interpreted in two ways. First, it may suggest that Montenegro was not perceived as an important geostrategic or economic partner during that period. Second, it is true that the aforementioned initiatives only materialised in institutional, diplomatic, and political forms in the second half of the 2010s. This assertion is supported by the economic data for the period 2016–2020, which places China in first place in terms of FDI inflow in Montenegro, with an average share of 9.6% of total FDI (Cental Bank of Montenegro, 2021a).

The lack of reliable data on Chinese investment in the Western Balkans has left room for different interpretations. The communication gap among Western Balkan countries regarding the surge in Chinese investment has further exacerbated this situation. All of this has led to increased concern on the part of the EU and the US. A prevailing narrative has been that such actions by the governments of these countries undermine Europe's political cohesion and open up space for "malign" Chinese influence. To gain a more nuanced understanding of this influence, it is crucial to emphasise that loans from Chinese banks do not equate to FDI from China into the Western Balkans. China predominantly focuses on infrastructure projects, not FDI per se. When these data are compared, the scope

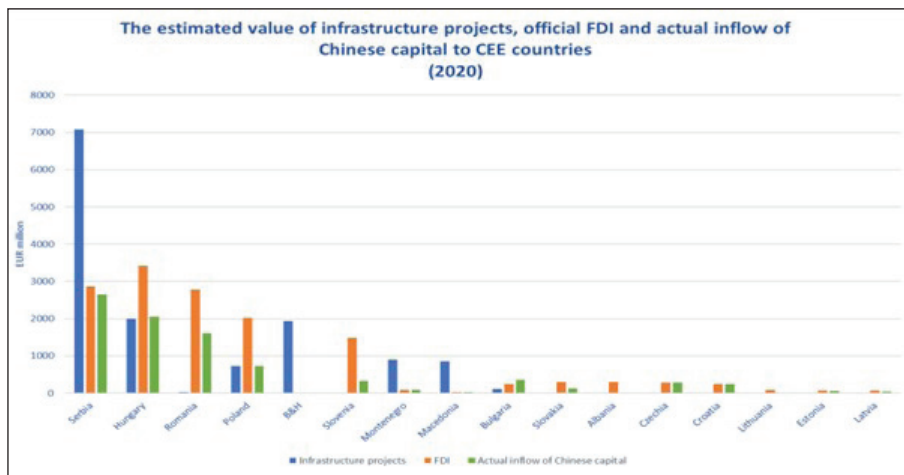


Chart 2: Comparison of China's infrastructure projects, FDI and the actual flow of capital in CEE countries (Source: Matura, 2021, 9).

of China's influence becomes somewhat clearer. In a comprehensive study, Matura compared the data on the number of infrastructure projects, FDI, and actual inflow of Chinese capital; upon analysing the chart below, it can be concluded that China's presence in this region is relatively limited (Matura, 2021).

The research considered here, spanning sixteen countries, concludes that investment from China actually plays a more important role in Western European countries than in any of the EU 17+1 members. On the other hand, Chinese investment is limited in this region, especially in countries that are already members of the EU. "Traditional European partners like Germany, other East Asian countries like Japan and South Korea and to a lesser extent the United States are still the most important investors" (Matura, 2021, 11). The only exception in the group of non-EU countries mentioned in the research is Serbia, which, in addition to infrastructure, has a substantial share of direct investments.

A HIGHWAY TO A DEBT TRAP?

In the economic sense, as Morrison states, Montenegro was the smallest and least developed republic of the former Yugoslavia (1945–1992). Its development relied to a large extent on the Yugoslav federal economic structures and federal subsidy programmes (Morrison, 2009, 76). The breakup of Yugoslavia also meant economic collapse and the disintegration of the single Yugoslav market, on which the economy of Montenegro depended significantly. Montenegro, as part of the state union of Serbia and Montenegro, was economically weaker, with a pronounced decline in employment levels

and an increasing number of workers financed from public revenues (Djuric, 2003, 144–146). Upon regaining its independence, Montenegro entered the process of transition and privatisation with a significantly weakened industry, relying to a large extent on tourism and services to prop up the economy.

In Montenegro, even before 2006 and the restoration of independence, questions were raised about the construction of the first kilometres of the highway. As early as 1969, there were plans to build a highway in Montenegro connecting Bar, a town and seaport in the south, to the north of the country, more precisely to Boljare, a village in Serbia and a state border crossing. During the communist period, Montenegro's infrastructural development was also emphasised. It was believed that better infrastructure in this small, hilly and then underdeveloped country would help break Montenegro's tribal particularism. Grgić (2017) explains that the reason for the construction of the highway was the desire of the political authorities in Montenegro to strengthen the sense of belonging to the state and the nation by connecting the north of the country with the south. A similar logic of thinking is presented by Dalakoglou in the case of socialist Albania, which also strengthened national unity through infrastructural development (Dalakoglou, 2010).

In more contemporary times, international Western creditors considered the construction of a highway in Montenegro unprofitable (Vukićević, 2021), even though the highway would connect with Corridor 11 and then to Corridor 10 (cf. Figure 2), highways built or planned in Serbia that would link Montenegro, especially the Port of Bar, with Serbia, then extending to Budapest and Zagreb, and



Figure 2: Corridors 10 and 11 (Source: Grgić, 2017, 7).

ultimately to Western Europe. By 2013, Montenegro had failed to find creditors willing to finance the construction of the highway. In 2009 and 2010, the Montenegrin government held unsuccessful negotiations with the Croatian company Konstruktor, which failed to secure the funds in time. Additionally, discussions with the Greek-Israeli consortium Aktor/HCH also proved fruitless, as the consortium failed to provide the necessary financial guarantees within the specified period (Kovačević, 2021). The only remaining option for the Montenegrin government was to turn to China, a recognised global leader in funding infrastructure projects, as the primary source of financial support.

The total length of the planned highway was 169.2 kilometres. Montenegro secured a loan from the Chinese EXIM Bank, valued at approximately 868 million US dollars, for the construction of the initial 41-kilometre-long Smokovac–Uvac–Matešev section (GEODATA, 2021). In the meantime, the funds necessary for the construction of this first section rose to 1.3 billion euros. This segment of the highway connects Podgorica, the capital of Montenegro, where one-third of the country's total population resides, with Kolašin, a town in the north of the country. This section is also the most costly due to the configuration of the terrain. The premise is that the highway as a whole would cost Montenegro around 1.7 billion euros (Arbutina, 2020). For comparison, Montenegro's budget for 2020 amounted to 4.779 billion dollars, and the debt associated with the highway, coupled with the pre-existing public debt, resulted in Montenegro having a 74.91% share of public debt in GDP in 2019 (Trading Economics, 2022). Montenegro's debt to Chinese creditors, stemming from the highway project, accounted for almost a quarter of Montenegro's GDP and threat-

ened the stability of public finances if it continued to grow.

Two independent financial sustainability assessments, one undertaken by the French company Louis Berger in 2009 and the other by the American company URS, indicated potential risks to the functioning of public finances and the sustainability of the project (Barkin & Vasovic, 2018). A third study was conducted in support of the project, but its findings were not published. The Law on the Highway, adopted in 2014, provided for significant concessions from Montenegro for the project, such as tax exemptions for construction works, labour, and imports associated with the highway construction (Preferential Buyer Credit Loan Agreement, 2014). Montenegro also assumed a considerable exchange rate risk by agreeing to accept the project financing in US dollars (Navarro et al., 2022). The contract with EXIM Bank stipulated an exemption from income tax for Chinese workers and Montenegrin companies involved as subcontractors. All these points are the matrix of the behaviour of a country in transition, actively seeking to attract investors by issuing state guarantees. This approach to financial dealings has been severely criticised in several European Commission reports on Montenegro's integration process (European Commission, 2018), and also by domestic institutions such as the State Audit Institution (Dabović & Pešić, 2013).

One of the most cited analyses, titled "How China Lends?" (Gelpert et al., 2021), also includes the example of Montenegro in order to prove the geopolitical character of Chinese financial affairs in different parts of the world. Although the case of Montenegro was not specifically addressed, the authors concluded that they "find widespread use of 'No Paris Club' and 'no comparability of treat-

ment' clauses – that expressly prohibit the borrower country from restructuring their outstanding debts to China in coordination with Paris Club creditors and/or on comparable terms with them" (Gelpern et al., 2021, 45).

The part that is particularly worrying and is at the core of the debt trap narrative is a clause (Article 5) within the contract. According to this clause, in case of non-payment of the debt, Montenegro waives its immunity based on sovereignty, except for military assets and property related to diplomatic-consular missions, within any possible arbitration procedure. In essence, that means that if Montenegro were to default on its debt, any and all state property or infrastructure, with limited exceptions, could potentially be seized by China, as the creditor, to satisfy the terms of the outstanding debt (Preferential Buyer Credit Loan Agreement, 2014). Precisely because of this vulnerability, Montenegro was listed as one of the eight highly endangered countries in a separate report by the Center for Global Development (Hurley et al., 2018).

REACTIONS TO MONTENEGRO'S CREDIT DEBT

The case of Montenegro has attracted the attention of Western institutions and researchers in particular. Most studies characterise the issue as a typical example of debt diplomacy. However, we believe that the case of Montenegro is rather an example of how a country in transition functions in the international financial and business environment. Borrowing from Chinese creditors was simply the most affordable option for Montenegro after years of searching for creditors. At the same time, narratives around China's desire to make Montenegro politically dependent can be dismissed immediately; this contention is further strengthened by Montenegro's NATO membership. The project, alongside the search for investors and creditors, was motivated by a clear multi-year political agenda in the country.

The fact that the highway was at the top of the political and electoral agenda of the then government in Montenegro is evident in the narrative that has been present in the Montenegrin public since 2014, referred to as "the project of the century" or "the national project that was only more important than the restoration of the independence of Montenegro" (Vijesti, 2017). At the time, President Milo Đukanović placed the responsibility for the highway and its geopolitical implications in the context of the EU's relationship with the Western Balkans region, stressing that Chinese capital was doing what the EU should be doing (B92, 2018). On the other hand, the intense response from the political opposition, segments of the professional

community, and the civil sector raised concerns about possible corruption, a debt crisis, and the catastrophic reflection of the debt on the sustainability of public finances. Consequently, the Movement for Change, then an opposition party, launched a petition calling for a referendum on the construction of the highway (Boričić, 2014). Furthermore, the NGO MANS filed a criminal complaint against the Ministers of Transport and Finance, alleging harmful behaviour during the conclusion of the contract for the highway construction project (Mina, 2014). After the change of government in 2020, ending the thirty-year rule of the Democratic Party of Socialists, the new government and the parties of the parliamentary majority viewed the completion of the construction of the highway as a significant success. The focus then shifted to publicising all contracts and assessing the potential environmental impact of the highway. Representatives of the new government made extensive use of media appearances to highlight the importance of the highway, again to strengthen their political agenda, particularly given that the highway became operational during their mandate. This is another indication that the various ruling structures viewed the highway as a compelling argument for their political relevance.

In mid-March 2021, the then Deputy Prime Minister of Montenegro, Dritan Abazović, asked the European Parliament's Committee on Foreign Affairs to help repay the loan. "Please help us to repay that money, to exchange that loan for a loan with a European bank, to conclude cooperation with a European financial institution, and to end Chinese influence", Abazović said at the time (Al Jazeera, 2021). Afterwards, Montenegro sent an official letter to the European Commission requesting the above-mentioned assistance (Tuhina, 2021). In response, the EU clarified that it could not aid Montenegro repay debts acquired from third parties (Radio Slobodna Evropa, 2021). Within the EU itself, Montenegro's debt issue triggered a debate about the bloc's strategic positioning in the Western Balkans. High Representative Josep Borrell emphasised the strategic importance of the Montenegro – China relationship, stating, "Montenegro is in the EU's backyard: it would be, finally, a concrete way to show that the EU is indeed a player, a true geostrategic actor, [and not] just the playground" (Ivković, 2021). After the EU's initial negative response in 2021, the Montenegrin government eventually made a hedging arrangement in cooperation with two American banks and one French bank. This arrangement reduced the interest rate on the debt owed to the Chinese Exim Bank from 2% to 0.8%, resulting in annual savings of eight million euros (Nyabiage, 2021). The issue of

Montenegro's debt resurfaced in July 2021 during discussions on Sino-US relations. The then Deputy Assistant Secretary of State of the United States of America, Matthew Palmer, assessed that the hedging arrangement protected Montenegro from the currency risk of the Bar-Boljare highway loan and that the reduced interest rate limited China's influence (RTCG, 2021). By contrast, in the domestic public debate, this financial arrangement faced criticism. Members of the Parliament demanded that the documents be made public, while analysts pointed out that after two years, depending on global financial trends, such an arrangement could mean either a profit or a loss for Montenegro's budget (DAN, 2021).

It is interesting that the actions of the EU, i.e. the expressed pragmatism towards Montenegrin debt, did not affect citizens' confidence in the EU. Support for membership remains extremely high, as does the assessment that Montenegro should rely on the EU to the greatest extent in its foreign policy (CEDEM, 2022). On the other hand, if we exclude the period of negative narratives about China during the COVID-19 pandemic, the percentage of those who evaluate China's role positively is stable at about 40%, placing China in second place just behind the EU and well ahead of individual Western countries (Kovačević, 2021, 7). In addition to the fact that issues related to China's debt diplomacy have been lost in the public debate, these data also indicate that citizens do not perceive the relationship between Montenegro and China as a factor that would disturb their attitudes towards the EU. However, we believe that the EU missed a significant moment to position itself as an important geopolitical actor, to indicate its sphere of influence, and to strengthen its soft power in Montenegro and the region by taking an active role in solving this problem. By contrast, the position of China in Montenegro is the result of a developed network of soft power instruments. As Tonchev argues, "the safest way to assess the effectiveness of China's soft-power strategy in WB countries would be a review of China's reputation, as reflected in opinion polls" and adds that according to some surveys "it is clear China is markedly more popular in the region [of South-east Europe] than in other parts of EU" (Tonchev, 2020, 19). There is almost no perception of the ideological framework in which China operates within Montenegrin public opinion, while public debates on China's domestic policy and respect for human rights are very rare. Political, cultural and economic cooperation, as part of a wider range of soft power, has only gained importance. Research from 2017 indicates that 56% of respondents believe that Montenegro would best achieve its

interests by strengthening ties with China (International Republican Institute, 2017). According to the same survey, China ranked third in the most desirable countries for investing in Montenegro, while 16% of respondents had the perception that China is the largest investor in Montenegro, just behind the EU in the first place. The previously mentioned evidence proves that in the years after the re-independence of Montenegro, China managed to build a favourable position in the public opinion and perception of Montenegrin citizens, indicating the influence and scope of its soft power in Montenegro. The enormous apparatus of China's soft power is based on building the image of a friendly state and a desirable economic partner that strives to achieve a win-win situation in every type of relationship without a "specific soft power strategy for this region" (Tonchev, 2020, 5). Based on the data shown, in the case of Montenegro, it can be concluded that this tactic has succeeded. The impact is based mainly on strengthening bilateral relations. Unlike developed democracies, such as North America, Germany, and Japan, where there is a very negative perception of Chinese influence (Nye, 2015), in Montenegro, a developing democracy, this is not the case. Due to the pronounced economic side of bilateral relations over the previous 15 years, we believe that this is another aspect due to which the Montenegrin authorities perceived China as a desirable highway creditor. That is why China's soft power strategy in Montenegro can be measured much more as a complement to its' economic presence than as a separate strategy per se. We understand this as a modified soft power concept in which economic power has taken on the aspects of soft power and is defined as commercial diplomacy in the context of soft influence.

CONCLUSION

In this scientific article, we investigated whether Montenegro is a target of Chinese debt diplomacy. We presented the economic relationship between Montenegro and China, and vice versa, along with the presentation of the most important parameters such as the volume of foreign trade and direct foreign investments. The primary focus of the work was on the financial debt arrangement that Montenegro agreed with the Chinese EXIM Bank in 2014, with the aim of building its first highway. The main conclusion of the research is that China did not conduct debt diplomacy towards Montenegro and that the request for indebtedness came from the Montenegrin side; thus, it was not in any way encouraged by China. In addition, we rejected claims suggesting that the Montenegrin Port of Bar would be a potential prey for China if Montenegro could not repay its debt.

When it comes to answering the first research question i.e. *How do the critics of borrowing relate to the wider issues of debt sustainability, financial stability and sovereignty of Montenegro?*, we believe that the answer lies not only in the Montenegrin debt to China but that it should be derived from wider scientific discussions. As explained in this paper, China has emerged as a major global lender, a policy initiated in the 1980s but only actualised in the first and second decades of the 21st century due to accusations of debt diplomacy and questionable intentions. As previously highlighted, related studies encompassing numerous examples of countries in Africa and Asia borrowing from China indicate that China behaves benignly and without ulterior motives. Therefore, from the perspective of Chinese lending practices, it would be unprecedented to attempt to seize part of Montenegro's national assets, in the hypothetical situation that Montenegro could not repay the loan. In the regional context, it would be short-sighted of China to risk compromising its international reputation by trying to annex part of the territory of Montenegro. We might also add to that the fact that the potential of China's soft power would be greatly harmed and that the gain would be disproportionately small compared to the reputation damage to China.

Montenegro, as a candidate for EU membership and a member of NATO, has successfully managed both to become part of the Western security architecture and to satisfy its need for Chinese financing. This experience could in the future serve as a model for cooperation between other small countries and China, particularly when these nations become integrated into security architectures distinct from China's.

As regards the second research question, i.e. *To what extent does borrowing affect relations between the European Union and Montenegro, bearing in mind the latter's integration process in the EU?*, Montenegro's debt to Chinese lenders has received a lot of attention within the EU. The EU was in a delicate position when Montenegro formally sought assistance, due to China's debt diplomacy. The EU could not help Montenegro directly, as this would have violated longstanding regulations governing how countries deal with loans from third parties. However, with the assistance of European and American banks, Montenegro was able to enter into a hedging arrangement that greatly helped it financially. Through this indirect aid, Montenegro continued to enjoy a form of EU protection. Apart from this episode, the transport infrastructure that China is developing in the Balkans and throughout Europe is supported by the EU. This is demonstrated by various joint transport improvement programmes, from which both Brussels and Beijing clearly benefit. Considering that Montenegro's highway project constitutes only a small segment of a broader road network, we conclude that the whole initiative is about the complementarity of EU and Chinese policies, with a reminder that Montenegro's stance towards the EU remains unchanged, despite the EU not directly intervening in the settlement of the loan issue.

The article analysed the economic relationship between Montenegro and China, in the light of the Montenegrin loan for the construction of its first highway. This loan served as a basis for claims that China is using debt diplomacy with Montenegro. This investigation paves the way for future research into the political relations between these two countries, the attitudes of Montenegrin citizens towards China through public opinion surveys, and the content of the narratives about China in the Montenegrin media.

PONOVNI RAZMISLEK DIPLOMACIJE DOLŽNIŠKE PASTI: ŠTUDIJA PRIMERA DOLGA ČRNE GORE DO KITAJSKÉ

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POVZETEK

V zadnjih letih je dolžniška diplomacija močno vstopila v politologijo in diplomacijo. Ker se zavedamo razširjenosti enostranskih pogledov na ta pojav, smo v prispevku želeli na novo osvetliti gospodarsko aktivnost Kitajske v Evropi z analizo odnosa s Črno goro na primeru izgradnje prve avtoceste v Črni gori. Pregled literature je s pomočjo znanstvene in javnopolitične analize omogočil celovit vpogled v izvor in razvoj tega pojava. Z obdelavo razpoložljivih primarnih podatkov smo opozorili na pomen raziskovanja gospodarskih odnosov med Kitajsko in Črno goro z vidika ekonomskih dejavnikov, kot so neposredne tuje investicije, zadolženost in javni dolg. Pokazali smo, da je Kitajska za Črno goro relevanten gospodarski partner in da poleg tega, da je največja posamična upnica, v Črni gori nima izrazitega gospodarskega položaja, ki bi ji dajal pomembno geostrateško lego. Z združevanjem ekonomskih in pravnih vidikov zadolževanja smo pokazali, da je ta poslovni odnos del notranjepolitičnega pomena in da so ga dominantno oblikovale politične elite v Črni gori. Z analizo smo izpostavili mednarodni pomen tega primera s poudarkom na odzivu EU in njihovi (ne)komplementarnosti s pobudami EU na Zahodnem Balkanu. Rezultati raziskave so pokazali znanstveno nevzdržnost kitajske dolžniške diplomacije na primeru Črne gore.

Ključne besede: Kitajska, Črna gora, diplomacija dolžniške pasti, mehka moč

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