

## What are the prospects for the new Chinese-led Silk Road and Asian Infrastructure Investment Bank?

**Mario Esteban** | Senior Analyst for Asia-Pacific at the Elcano Royal Institute | @wizma9.

**Miguel Otero-Iglesias** | Senior Analyst for the International Political Economy at the Elcano Royal Institute | @miotei.

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### Theme

The new Silk Road is the most ambitious international initiative yet to be launched by the Chinese President, Xi Jinping. This policy has many strands, one of the most prominent being the creation of the Asian Infrastructure Investment Bank. We examine its possible implications for Europe, including Spain.

### Summary

China is using the new Silk Road as a means of positioning itself to play a decisive role in the integration process of Eurasia. The project promises to be an inclusive one, in which there will be space for all types of political regimes and actors, both public and private, based on a market logic that looks set to enable all participants to benefit. It is not therefore a case of an altruistic initiative, nor is it an exercise in development aid. The Chinese leadership believes that the implementation of this plan will help it secure a range of key objectives in domestic and foreign policy. The initiative is not free of risks for the EU, which could see its international influence eroded; meanwhile, corruption and indebtedness have the potential to destabilise such sensitive regions as the Balkans, Eastern Europe, the Middle East and Central Asia. The only means of avoiding this is if European governments and societies subscribe to the project in a critical and constructive spirit, helping to shape it and thereby ensure that it does not become a conduit solely for economic growth, but also for development.

## Analysis

No state-backed project has garnered as much media attention this year, whether inside or outside China, as the new Silk Road, the most conspicuous aspect of which will be an extensive network of communication and transport infrastructure, both new and renovated, to improve connectivity between China, the rest of Eurasia and Africa. Launched towards the end of 2013, the programme encompasses two main initiatives: a Silk Road Economic Belt and a 21<sup>st</sup>-century Maritime Silk Road. The former aims to improve overland connections, while the latter focuses on maritime routes. Other plans mooted are directed at upgrading energy links and information super highways. In October 2014 the creation was also announced of the forthcoming Asian Infrastructure Investment Bank, operating within the same framework; set to have an initial capital of up to US\$100 billion, this signals the start of a new era in the international financial system, where the traditional powers no longer play the lead role when it comes to adapting to the structural changes taking place in the global economy.

Beijing hopes to use this plan to strengthen its economic, political and cultural ties with the rest of the States involved. In the commercial arena for example, estimates from the Chinese government envisage that the US\$1.25 trillion worth of trade China conducted with Eurasian countries in 2013 will double by 2020. Furthermore, the initiative will not only reinforce China's bilateral relations with a large number of States, with the ensuing boost to her international stature, it will also enable Beijing to drive various domestic priorities and significantly enhance its influence over the integration processes underway within the macro-region.

The project is still in its earliest phase and clearly exhibits many profound difficulties, but its potential for having an impact of historic proportions on the development of Eurasia means that it merits rigorous analysis. This task has been made easier by the significantly greater information about the new Silk Road that has emerged over the last few months, especially with the recent publication of an official action plan.<sup>1</sup>

### *Road map of a project*

Both the overland and maritime aspects of the new Silk Road include multiple routes, which in many cases complement each other. The main difference between the two is that the maritime routes are already much more developed and are used to transport a much larger volume of trade.

In the terrestrial sphere the emphasis is being placed on railways and various routes are being developed to strengthen links between China, Central Asia and the EU (either through Russia and Belarus or through Iran and Turkey), and between China and the Indochinese Peninsula. This great overland corridor, which would connect the two extremities of Eurasia from east to west, would be complemented by other

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<sup>1</sup> Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road, [http://en.ndrc.gov.cn/newsrelease/201503/t20150330\\_669367.html](http://en.ndrc.gov.cn/newsrelease/201503/t20150330_669367.html).



In the maritime sphere, the current route connecting Chinese ports with Europe, passing through the Western Pacific and the Indian Ocean before reaching the Mediterranean Sea, will be maintained; other routes, not yet opened, would avoid the Strait of Malacca by setting out from ports in the Indian Ocean. Although no details have been revealed, in all likelihood these ports belong to countries with which Beijing enjoys close diplomatic relations, such as the port of Gwadar in Pakistan, operated by a Chinese company, or Chittagong in Bangladesh. The map published by the official Xinhua news agency also shows a connection with Kenya, where Chinese companies are building various infrastructure projects to improve both internal transport links as well as those with neighbouring landlocked countries such as Ethiopia, South Sudan, Uganda, Rwanda and Burundi. In the case of Europe it is envisaged that the lead role will be played by the port of Piraeus, both because of its location and the involvement of the Chinese company COSCO Pacific, part of the Chinese state enterprise China Ocean Shipping Company. COSCO Pacific has been operating the freight terminal at Piraeus since 2008 and has announced an investment of €230 million to increase its capacity to 6.2 million containers, and is also one of the five finalists in the current privatisation of 67% of the Piraeus Port Authority. It is important to bear in mind that the development of ports often goes hand in hand with developing the railway infrastructure leading to the port, so as to avoid bottlenecks. As far as Spanish ports are concerned, China sends more goods through the ports of Barcelona and Valencia than any other country, and is ranked second at the port of Algeciras. The most significant development envisaged in the short term is the investment of €150 million by Hutchison Port Holdings to extend the Barcelona Europe South Terminal, opened in 2012.

### *The Asian Infrastructure Investment Bank*

There is a wide international consensus that pinpoints lack of infrastructure as one of the main obstacles to economic growth among the less-developed countries comprising the new Silk Road. This diagnosis is by no means new; nor is it novel to identify lack of capital as the main reason for this shortfall not having been remedied. It is hardly surprising therefore that the new Silk Road should come equipped with financial measures designed to tackle this situation. Some of these measures are directly linked to the project, such as the Silk Road Fund, set up with US\$40 billions and jointly founded by the Chinese currency reserves, the China Investment Corporation (the largest Chinese sovereign wealth fund), the Export-Import Bank of China and the China Development Bank; other institutions, such as the Asian Infrastructure Investment Bank itself, the China-ASEAN Investment Cooperation Fund and the China-Eurasia Economic Cooperation Fund, can finance projects that fall within the new Silk Road project, although their scope and frame of reference is wider.

Such mechanisms are clearly inadequate, however, if the project's viability is to be ensured. Even the figure of almost US\$4 trillion amassed by China in its currency reserves pales into insignificance in the context of the US\$21 trillion some international experts reckon it would cost to make the new Silk Road a reality, or the US\$8 trillion the Asian Development Bank thinks Asia will need to invest on infrastructure before 2020. Inevitably, in the light of the sums being mooted, the Chinese authorities have made it clear that the plan does not rely on donations, but rather investments made in accordance with market criteria. From this perspective it is envisaged that both States and participating companies as well as private international investors will be able to provide financing for the project via a number of different routes.

Herein lies one of the chief unknown quantities that will determine what impact the new Silk Road ultimately has. It hardly needs to be said that several of the States involved in the project do not exactly shine when it comes to good governance; on the contrary, they suffer from high levels of corruption and a political class that has a proprietorial attitude towards the State. How have projects that have not hitherto elicited the interest of private investors going to attract them now? How is it possible to finance these projects without it leading to a substantial increase in the international debt burden of the countries where the infrastructure is to be built? At the very least, how can it be guaranteed that the debt will contribute to the development of the countries in question, rather than lining the pockets of elites? In this context, the signing up of 18 member-countries of the OECD's Development Assistance Committee, Spain being one of them, as founder members of the Asian Infrastructure Investment Bank is extremely good news. Furthermore, the Chinese government itself seems to have toned down its non-interventionist rhetoric and is referring to the desirability of creating supervisory mechanisms for the investments and coordinating economic policies to ensure the success of the project.

### *Unfortunate parallels*

Although the Belt and Road initiatives were announced in September and October 2013 respectively, the fact is that they have suffered from a palpable lack of precision, at least until the latter part of March 2015 with the publication of the official action plan. The uncertainty surrounding the nature of the new Silk Road generated wide-ranging speculation about its content, and it was not unusual to read non-Chinese analysts comparing the new Road to the sinocentric vassal system of imperial China and to the Marshall Plan. Both comparisons should be treated with great caution, however, since they obscure as much as they enlighten. At various times at the height of imperial China, the empire was able to lead a hierarchical system of international relations, whereby various neighbouring nations paid tribute to the Chinese Emperor in recognition of his authority. While it is clear that Beijing exerts more and more influence over its neighbours, there is absolutely no possibility that this will lead to a relationship similar to the sinocentric system because, apart from anything else, China ceased to enjoy the self-sufficiency needed to drive its own socioeconomic development some time ago. The mutually



dependent relationships that China has established with the outside world ensure that relations as hierarchical as those of the tribute States are simply not viable. As far as the Marshall Plan is concerned, there are two essential differences. The new Silk Road is not an aid plan; instead, it is governed by market criteria, and its character is inclusive, since no State will be prevented from participating on the grounds of its political regime. It has even been confirmed that Taiwan, which had already applied to join the Asian Infrastructure Investment Bank, will be welcome. In other words, the Chinese project neither submits to a bloc-based analysis nor is it a zero-sum game, although clearly this does not entail that it lacks objectives of a geopolitical nature.

### *Significance for China*

The new Silk Road started to acquire increasing prominence in the latter part of 2014, with constant references being made to the project both at the main political events within China –witness the latest plenary sessions of the National People’s Congress and the People’s Political Consultative Conference– and at high-level meetings between Chinese leaders and their Eurasian counterparts. Moreover, the creation of a leadership group to direct and oversee the implantation of the Belt and Road policies has just been announced.

The way the new Silk Road has been promoted to the top of the agenda is a reflection of its priority for Xi Jinping as a means of achieving key goals in domestic and foreign policy. Maintaining China on the path of economic development is the priority both for China’s leadership and its citizens and this project can contribute to such development in at least four ways: driving the internationalisation of its construction industry, encouraging exports, reducing risks in the supply chain and attracting investments towards the interior of the country.

The construction industry has become one of the main drivers of economic growth and employment in China in recent years. This is due in part to the billions the Chinese authorities have invested in infrastructure projects as a way of kick-starting the economy amid the international slump in demand triggered by the global economic and financial crisis of 2007-09. The problem is that the fillip derived from construction is losing steam, owing to a slowdown in the property sector, problems of over-supply and the sharp increase in domestic debt, especially on the part of local governments, which shoulder much of the burden of the infrastructure projects. The solution lies in stepping up the already significant internationalisation of Chinese construction companies, and nothing is more likely to achieve this end than the myriad multi-million dollar infrastructure projects generated in the wake of the new Silk Road.

With regard to encouraging Chinese exports, the Silk Road project is not confined to constructing infrastructure. It is also committed to strengthening trading links between the participants by creating free trade areas and eliminating non-tariff barriers, and the speeding up and harmonisation of administrative processes such

as customs procedures. All this is imbued with a logic aimed at extracting the maximum benefit from the comparative advantages of the various participating States, something that the Chinese government hopes will act as a catalyst for its exports.

The way China's economy operates is highly dependent on imports (energy sources and raw materials) and long-haul exports that in many cases travel via routes that the Chinese neither control nor are capable of controlling. This generates strategic vulnerabilities for China in the event that certain key points, such as the Strait of Malacca, should ever be closed to Chinese commerce. With the prospect of the diversification of routes offered by the new Silk Road, there is a substantial reduction in these strategic risks vis-à-vis several of China's main raw material and energy suppliers and its largest customer, the EU, as well as the Atlantic coast of the US. In many cases the new routes would also entail time savings.

It is also thought that the new Silk Road could help to attract investments in labour-intensive industries to China's interior. Eastern China has been attracting investment in labour-intensive production processes for decades. This trend has stalled in recent years, however, due to the sharp upturn in salary costs. Rather than seeing these activities being transferred to other countries, such as Vietnam, the preferred scenario for Beijing is for them to go to the Chinese hinterland, where labour costs are appreciably lower than on the coast. The proposed Silk Road would significantly increase the connectivity of various inland regions, making it much more attractive for foreign businesses to invest in them.

This last point would not only contribute to China's macroeconomic development but also give a boost to inter-territorial cohesion, a highly sensitive subject because of the yawning chasm that exists in the levels of development between different areas of the country and especially because of the existence of significant separatist movements in Tibet and Xinjiang. Indeed, as gateway to Central Asia and Pakistan, one of the regions that stands most to benefit from the Belt is precisely Xinjiang itself. This appears particularly promising to the Chinese authorities, who perceive modernisation in the region as the ideal antidote to separatism.

The reformist language used in the official plan of action, which proposes forms of economic liberalisation that go beyond the current Chinese reality, for example as regards the services sector or the role played by the market in the distribution of resources, suggests that Xi Jinping may be contemplating using the Belt and Road policies to push through internal reforms that generate friction within certain quarters of the regime. Moreover, this link between the new Silk Road and the need to drive through more internal reforms is explicitly made in the project's official plan of action. It thus seems that President Xi may be following the same strategy as Jiang Zemin and Zhu Rongji, when China's admission to the WTO served them as a means of introducing liberalising reforms in the teeth of internal opposition.

In addition to these domestic goals, there are others more closely tied to Beijing's international strategy. If the project becomes reality, it will help to generate greater economic integration both within Eurasia and between Eurasia and Africa. The fact that China is leading the project ensures that it occupies an enviable position for increasing its international influence when the financial and trade flows between the countries in these regions and Beijing start to build up. In the financial field it would not only contribute to the internationalisation of the renminbi, with the prospect of various participants in the new Silk Road, both public and private, issuing bonds in the Chinese currency; interest in the Asian Infrastructure Investment Bank among the international community, including some of Washington's traditional allies, throws an even stronger spotlight on the US congressional veto of reform of the International Monetary Fund.

Particularly significant in terms of security is the strengthening of ties with Central and South East Asian countries, which are crucial for China in tackling such challenges as separatism, terrorism, drug trafficking and a range of territorial disputes. China is also aware that it will be much easier to become a regional leader if it manages to quell the alarm with which several neighbours view its re-emergence. Initiatives like the new Silk Road and the Asian Infrastructure Investment Bank seek to induce other players on the international stage, especially some of China's neighbours and the traditional powers, to stop interpreting China's ascent as a zero-sum game and start seeing it as an opportunity in which all stand to benefit. This would be the case for less wealthy countries because China would be playing the role of financial and technological facilitator, helping to overcome one of the main bottlenecks holding their development back: the lack of infrastructure. As for the traditional powers, these too would benefit from the prospect of business opportunities and a more stable international climate, courtesy of the socioeconomic progress that would be made by less-developed countries and a greater degree of interdependence between a range of international players (whether States or otherwise).

### *Implications for Europe*

In the event that it becomes a reality, the new Silk Road will have multiple repercussions for Europe of an economic, geostrategic and geopolitical nature. The economic impact is likely to be the most obvious and will be fundamentally positive by dint of generating multiple opportunities for European businesses, both in China itself and in other countries on the route of the Belt and Road, and reducing costs for consumers. The primary beneficiaries of these opportunities will be construction, transport and logistics companies, which will have the chance to secure the building and operating contracts for the new infrastructure. The process is open not only to Chinese companies –as the German-Russian consortium, Trans-Eurasia Logistics, which operates container traffic between China and Germany via Russia, demonstrates– but also to European investors and companies.



The infrastructure projects will in their turn pave the way for European exports and investments in areas with high potential for economic growth, such as inland China, where GDP is growing faster than in coastal areas, and East Africa. The advent of such export and investment opportunities will be due not only to the greater degree of connectivity engendered by the new infrastructure but also to the liberalising measures of an administrative nature that the Road seeks to institute both within and beyond China's borders, and which are in line with the approach adopted by European diplomacy. It is important not to lose sight of the fact that the development model on which the initiative relies, as is evident from the action plan published by the Chinese government, is based on liberalisation, internationalisation and economic diversification.

Furthermore, there are certain countries in Europe, particularly Greece and some of the members of the cooperation forum that Beijing runs with central and eastern European countries (CEE), known as the 16+1 group, which will be able to use greater Chinese investment to construct terrestrial and maritime infrastructure related to the new Silk Road. Notable in this respect is the successful extension of the freight terminal in the port of Piraeus, which has triggered the need to upgrade the rail connections between the port and Central Europe; this in turn has led to the announcement of a high-speed line between Belgrade and Budapest, scheduled to be finished in 2017 and subsequently extended to Athens. More speculatively, certain news outlets in China have reported possible plans by the Chinese authorities to develop a high-speed line that would connect Beijing with London, passing through Kazakhstan, Uzbekistan, Turkmenistan, Iran, Turkey, Bulgaria, Romania, Hungary, Austria, Germany, Belgium and France. On the other hand, ports in the north of Europe could lose importance if the connections between China and other parts of Europe improve. By the same token, it is possible for the new infrastructure being mooted in the Middle East and Africa to create a situation in which many of the supply routes that start or terminate in these regions cease to pass through Europe.

The establishment of new routes looks set to reduce transport costs and lead times, but also risks. With the diversification of transport routes, the chances of a disruptive event significantly altering the flows of goods within this macro-region diminish. Meanwhile the geostrategic value of specific areas, such as the Strait of Malacca on the maritime route, and Russia on the overland route, is reduced. All this is clearly positive for Europe.

Also positive is the fact that the project is based on an inclusive approach, one that fosters interdependence and shared development, rather than competition between blocs, by dint of strengthening all manner of ties between participating countries. It is a matter of driving trade and investment, but also academic, scientific and cultural exchanges and building bridges between the societies on the paths of the Belt and the Road. This is how the great majority of China's neighbours have read the situation, having signed up to the initiative despite the fact that several of them have

running territorial disputes with Beijing. The only important players who have not signed up are the US and Japan, out of preference, and North Korea, because the Chinese government believes that Pyongyang does not provide the necessary information about its economic situation.

In addition, it embraces one of the founding principles of the EU: the positing of regional integration as a source of prosperity and stability. Brussels, with its consistent track record of supporting integration processes that are taking place in the region, ought to follow suit here, especially in light of the fact that it is a process that involves Europe itself and in which it is welcome to participate in an active way. Europe needs to have a presence in a project it can help to mould, so as to ensure it becomes a source of prosperity and stability not only for the Old Continent itself but also for its neighbours, with the ensuing dividends in terms of security and economic opportunities for European society.

### **Conclusions**

The new Silk Road is a project of great potential that reveals a version of China that is prepared to lead major initiatives on the international stage without succumbing to an exclusionary approach. European governments and societies should sign up to this project in a critical and constructive spirit to help give it shape, avoiding getting sucked into a bloc-based rivalry that has been rendered obsolete by an international order characterised by globalisation and interdependence.