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POLICY INSIGHT

The Belt and Road Initiative: Motivations, financing, expansion and challenges of Xi's ever-expanding strategy

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ABSTRACT

The paper examines the motivations, financing, expansion and challenges of the Belt and Road Initiative (BRI). The BRI was initially designed to address China's overcapacity and promote economic growth in both China and in countries along the "Belt" and "Road" through infrastructure investment and industrial capacity cooperation. It took into account China's strategic transition in its opening-up policy and foreign policy to pay more attention to the neighboring countries in Southeast Asia and Central and West Asia when facing greater strategic pressure from the United States in East Asia and the Pacific region. More themes have been added to the initiative's original framework since its inception in 2013, including the vision of the BRI as China's major solution to improve international economic cooperation and practice to build a "community of shared future for mankind", and the idea of the Green Silk Road and the Digital Silk Road. Chinese state-owned enterprises and policy and commercial banks have dominated investment and financing for BRI projects, which explains the root of the problems and risks facing the initiative, such as unsustainable debt, non-transparency, corruption and low economic efficiency. Measures taken by China to tackle these problems, for example, mitigating the debt distress and improving debt sustainability, are unlikely to make a big difference anytime soon due to the tenacity of China's long-held state-driven investment model.

Keywords: *BRI; overcapacity; infrastructure investment; industrial cooperation; financing; state-owned banks; ever-expanding strategy; debt trap; debt sustainability*

1. Introduction

The Belt and Road Initiative (BRI), China's investment plan to build a complex global infrastructure network connecting Asia, Europe and Africa, has attracted extensive attention in the six years since its initiation in 2013. Chinese capital-dominated investments in a large number of infrastructure projects in Southeast Asia, Central Asia, Eastern Europe and Africa brought about economic growth and job opportunities in recipient countries, while receiving lots of controversy and criticism, such as being called a "debt trap" and "new colonialism" from Western countries. In any case, the BRI has stirred the global economic and political order in a very Chinese way by signing up 131 countries to participate in China's global infrastructure investment project by the end of April 2019 (Belt and Road Portal, 2019). It drew even wider attention and a more intense response from the world when Italy signed a memorandum of understanding (MoU) with China on

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March 23, 2019, and became the first Group of Seven (G7) major economy to officially join China's ambitious infrastructure project.

Enlisting Italy in the BRI just before the second international BRI Forum (BRF), held in April 2019, was deemed a symbolic victory and landmark achievement for China. As the first G7 country to join the BRI, Italy's enrollment makes the forum look more appealing in the international community. The second BRF officially indicated the end of phase one of the BRI expanding into the world and the beginning of a new stage, featuring careful review, assessment, practices and risk management for BRI projects. Before that, President Xi's remarks on the fifth anniversary of the BRI in 2018 implicitly announced the beginning of this transition. Using a metaphor, Xi described the BRI's first five years of development as the freehand brushwork in traditional Chinese paintings and the next phase of the BRI as a Gongbi painting, which is characterized by close attention to details and a realistic style. At this juncture, a review of the development and evolution of the BRI over the past six years provides a full-scale view of the initiative and sheds light on how China might respond to future controversy and criticism.

The paper will first examine the policy-making process of the BRI by exploring the motivations behind the plan President Xi proposed and how the initial Silk Road projects have developed into China's package of strategies over the past few years. The second part of the paper will discuss the priorities and performance of China's investments in the BRI from the angles of geographical distribution, routes and projects, priority sectors and the connection between the BRI and the previous "going out" strategy China started at the beginning of the twenty-first century. The model and the specific ways China finances and invests in BRI projects, to a great extent, decided the nature of the China-led global infrastructure investment plan. The third part of the paper will review BRI financing in detail. Based on the geopolitical and geo-economic analysis of the BRI in the previous parts, the fourth part will reveal the implications of the BRI for global governance as it goes beyond the ambitious infrastructure investment plan. The fifth part of the paper will address the risks and problems facing the BRI and the controversy and criticism it has encountered. The final part of the paper will summarize the BRI's ever-expanding themes and the problems and risks it faces, and their implications for the future of the BRI.

2. The policy-making process of the BRI

2.1. Motivations

The origins of the BRI can be traced back to 2012, when overcapacity emerged as a serious challenge to China's industrial and economic structure (Xinhua, 2012). The huge stimulus package adopted in 2008 has created and exacerbated the existing issue of excess capacity, although it helped sustain the country's economic growth through the global financial crisis. During the period of 2008–2012, Chinese economists (National Business Daily, 2009; Jin, 2012; Bao, 2012) talked about a new Marshall Plan or a Chinese version of the Marshall Plan—a global infrastructure investment proposal in which China can actively participate and help boost the world economy and take a lead in infrastructure investment in developing countries while providing a solution to its domestic overcapacity. The new Party chief, Xi Jinping, listed overcapacity as the top priority for strategic economic restructuring (Xinhua, 2012) at the first Central Economic Work Conference in December 2012, two months after the Party's 18th National Congress was held.

The idea of a Chinese version of the Marshall Plan only gained momentum when it was combined with the strategic changes in China's opening-up policy and foreign policy, as well as the existing domestic development project, the Western Development Strategy. Wang Jisi's 2012 article was the first to combine the concerns of domestic economic growth and national security into one strategic move by suggesting China "march westward" to address both concerns (Wang, 2012). The idea expressed in this article was regarded as the academic source for the ideas of the Silk Road Economic Belt and the 21st Century Maritime Silk Road proposed in the following year.

Reform and opening up have been China's fundamental national policy since the end of the 1970s, with its priority of opening up to developed economies to gain access to export markets, technology and investment. Opening economically and strategically toward its western border was a revolutionary change in China's foreign economic policy and global strategy when China became the world's second-largest economy in 2010, with excess capacity and capital. The focus of the opening-up policy on the bordering countries in Central Asia, South Asia and Southeast Asia aligns with China's goals of outward investment, capacity export, "good neighbor" foreign policy and the Western Development Strategy.

The performance of the Western Development Strategy, announced in 1999 when China's top leaders began to push the country's backward remote regions to catch up economically with its developed coastal areas, had not been impressive. Under the changed circumstances, the western development program was resurrected in the name of advancing an all-around opening-up policy and became the domestic component of the new Silk Road plan aiming to develop the western region of China, which lagged behind the rest of the country, as a solution to the imbalanced economic development.

China's new Silk Road plan also takes into account the efforts to ensure national security and energy supply security. Maintaining stability and security in Xinjiang and guaranteeing oil and gas supply security from Central Asia have long been two priorities in China's policy in this area.

Since 2009, the security situation in Xinjiang has been deteriorating, with growing radicalization and national separatism among the majority Muslim population there. Anti-national separatism and upholding national unity have become the ongoing top priority in Xinjiang since then. A series of violent attacks in Xinjiang in April and June 2013, just three months before President Xi proposed the new Silk Road plan in September in Kazakhstan, caused extreme concern for top Chinese leaders about the stability and security in Xinjiang (Xinhua, 2013a). In December 2013, Xi convened the second Politburo Standing Committee (PBSC) exclusive meeting on Xinjiang issues after two more violent attacks happened in Xinjiang (Ta Kung Pao, 2014). Xinjiang was designated as the core region for the Silk Road Economic Belt, and Xinjiang's development was integrated into this national strategy after Xi paid a visit to Xinjiang in April 2014. During his visit, Xi called for the whole Party and state to support Xinjiang's development and stability. Xi and other Chinese senior leaders believed that being underdeveloped is the biggest potential threat to stability and security.[1] They maintained that the new Silk Road plan would be beneficial to the stability and security in Xinjiang by promoting economic growth and integration with its bordering Central Asia

[1] Chinese Vice Minister of Foreign Affairs Le Yuchen expressed this opinion when interviewed by the Financial Times in 2018. See the transcripts of the interview on the website of China's Ministry of Foreign Affairs: www.fmprc.gov.cn/web/wjbxw_673019/t1598794.shtml.

countries (People's Daily, 2014).

The Silk Road plan was expected to integrate the elements of investment, trade, energy and national security into one project to meet all goals. The Western Development Strategy contains elements of addressing the security and stability in Xinjiang through infrastructure investment and economic growth. The Silk Road plan also overlaps with the crucial routes and energy pipelines to guarantee China's energy supply in Central Asia, in particular, Kazakhstan and Turkmenistan. Since it shares geographical borders with Central Asian countries, Xinjiang is a key region in guaranteeing the smooth operation of these pipelines and energy transport routes for shipping oil and gas into China.

A Chinese version of the Marshall Plan as China's overseas infrastructure plan was not built from nothing. Through its rapid increase of investments in energy- and resource-rich countries in Central Asia, the Middle East and Africa, the existing "going-out" strategy since the beginning of the twenty-first century had already laid a solid foundation for China's new Silk Road plan, which could be a version 2.0 of the outward investment strategy.

The idea of a new Silk Road plan was believed to be an adjustment of China's grand strategy in foreign policy in response to the US "pivot to Asia" policy since 2010. The United States proposed a new Silk Road plan for strategically important Central Asia in fall 2011, and US Secretary of State Hillary Clinton had actively advocated for the US version of the Silk Road plan. Under pressure both from the US pivot to Asia policy and the Trans-Pacific Partnership initiative, as well as the direct impact of the United States' new Silk Road plan, Chinese policy-makers needed to think of ways to respond strategically. The Ministry of Foreign Affairs invited scholars to discuss how to respond to the US new Silk Road plan in 2012.[2]

A meaningful adjustment in China's foreign policy to devote more attention to its peripheral diplomacy and build what President Xi described as community diplomacy among China's neighboring countries in Central Asia, South Asia and Southeast Asia is believed to have inspired the proposal of the new Silk Road plan. It does not seem a coincidence that President Xi proposed the new Silk Road plan in September and early October of 2013 and then unprecedentedly convened China's first high-level meeting on peripheral diplomacy at the end of October. The adjustment demonstrated Xi's strategic pivot to China's Asian neighbors, forging an Asian community based on connectivity in infrastructure, trade, currency, policy coordination and cultural exchanges. This policy pivot was expected to ease neighboring countries' worries and fears of China's rise and help China promote regional economic integration with neighboring nations.

All things considered, the proposal of the new Silk Road plan represented a significant rise in the importance of peripheral diplomacy in China's foreign policy and constituted an important part of its domestic economic growth strategy. The new Silk Road plan eventually evolved into a significant foreign economic policy and grand strategy, i.e., the BRI in 2015, and many other factors and elements were added to the initial ideas of the new Silk Road plan in the following years. The years 2013 to 2015 were the key period to observe how the initial Chinese-version Marshall Plan evolved into Xi's grand outward investment plan to address both economic growth and national

[2] The author was invited to a dialogue with senior officials from the Bureau of Asian Affairs under the Ministry of Finance (MoF) in 2012.

security concerns.

2.2. Timeline of the policy-making process

President Xi Jinping proposed the idea of the Silk Road Economic Belt in a speech in Kazakhstan on September 7, 2013. Less than one month later, Xi raised the idea of the 21st Century Maritime Silk Road in Indonesia when attending the Asia-Pacific Economic Cooperation meeting on October 3, 2013. In hindsight, Kazakhstan—a typical country on the Belt—and Indonesia—a symbolic nation for the Road—were purposely chosen prior to announcing China's ambitious Silk Road plan.

One month later, the Silk Road Economic Belt and the 21st Century Maritime Silk Road were written into the Decision of the Third Plenary Session of the 18th Party Congress (Xinhua, 2013b), Xi's economic growth blueprint since he assumed the presidency of China in March 2013, meaning that the Silk Road plan became the party's official policy. This demonstrated that the initial idea of the BRI was an approach to China's close relations with its neighboring countries via close economic connections and marked the beginning of the Silk Road plan's evolution into President Xi's signature foreign policy in the coming years.

On November 6, 2014, the Central Leading Group on Financial and Economic Affairs, the highest body in China's economic policy-making and headed by President Xi, convened a meeting on the Silk Road Economic Belt and the 21st Century Maritime Silk Road. The establishment of the Asian Infrastructure Investment Bank (AIIB) and the Silk Road Fund was declared at the meeting. This meeting at the highest level used the name "One Belt and One Road" instead of Silk Road, indicating that the BRI had evolved into China's new grand plan and included goals in both economic integration and foreign policy adjustment with countries along the Belt and Road (Xinhua, 2014).

Noticeably, at the meeting Xi described the AIIB as a multilateral bank to finance the infrastructure in countries in the BRI and the Silk Road Fund as China's direct financial support for the BRI. It turned out, however, that the establishment of the two financial institutions was more symbolic for BRI financing. They only accounted for a small part of the financial resources supporting BRI projects in the following years. The China Development Bank (CDB) and Exim Bank of China became the major financing sources for the BRI, together with the support from the other four big state-owned commercial banks, in particular the Bank of China and the Industrial and Commercial Bank of China (ICBC).

The following year, the party's highest executive agency of the BRI was set up and the road map for the BRI was announced. On February 1, 2015, the establishment of the Central Leading Group for Advancing the Development of the BRI was announced. Headed by Vice Premier Zhang Gaoli and including three other members of the PBSC, the leading group was to implement the BRI by serving as the coordinating mechanism. The office of the leading group was established at the National Development and Reform Commission (NDRC) and four working groups were established under it. On March 28, 2015, the NDRC, the Ministry of Foreign Affairs and the Ministry of Commerce, with State Council authorization, announced the official road map of the BRI: "The Vision and Proposed Actions Outlined on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road".

In 2016, the BRI was further integrated into China's national economic blueprint. It was designated as the leading program for the new vision of China's opening-up policy outlined in China's 13th Five-Year Plan (2016–2020) in March. There is one chapter in the plan that exclusively focuses on the BRI (NDRC, 2016). Four months after the first BRF was held in May 2017, the BRI was written into the constitution of the Communist Party of China at the Party's 19th Congress in October. This action implied that the BRI is one of the key foreign policies in the Party's long-term grand plan, and that politically it will be carried out even after President Xi is no longer in power.

During a government reshuffle in March 2018, a new ministerial-level agency, the China International Development Cooperation Agency, was established, with implementing the BRI as one of its goals. This development indicates that the BRI was further established as a part of China's grand plan of global governance and is a key component of China's efforts to contribute to international development.

3. China's Investments in the BRI: Priorities and Achievements

3.1. Priorities

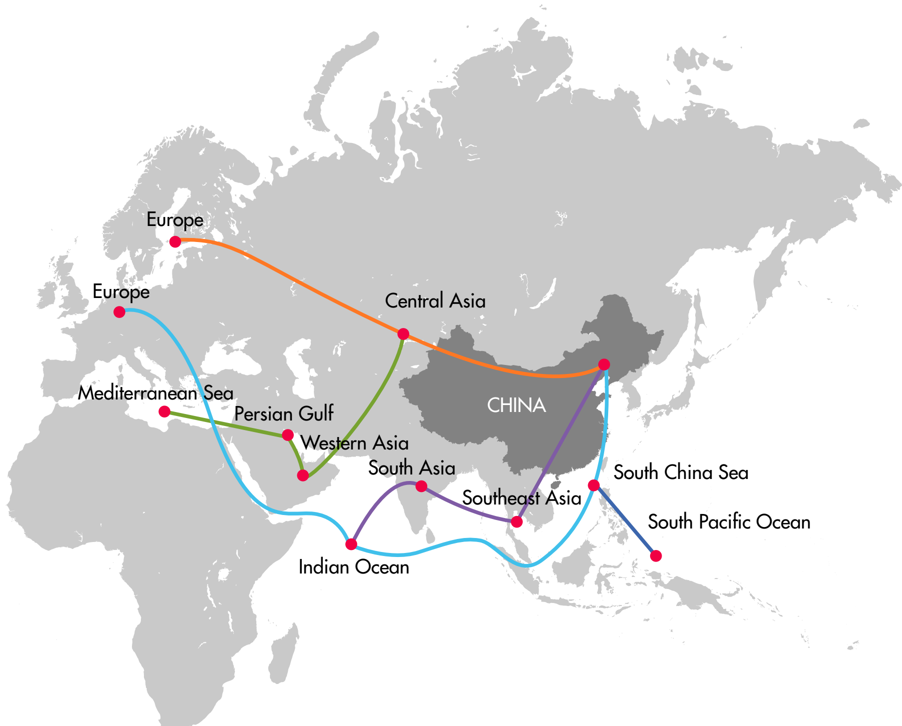
"The Vision and Proposed Actions Outlined on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road" listed five priorities in principle: policy coordination, facilities connectivity, unimpeded trade, financial integration and people-to-people bonds (NDRC, 2015). Based on where the money actually goes, the priority is on infrastructure connectivity and capacity cooperation, with particular focus on infrastructure projects in transport (rail, highway, port, shipping) and energy (hydro, oil and gas, coal) (see **Table 1**). The top two priorities of infrastructure connectivity and capacity cooperation are also in accordance with the directions for outward investment defined in the Guiding Opinions on Further Directing and Regulating the Direction of Overseas Investment that was jointly issued by the NDRC, the Ministry of Commerce (MOFCOM), the People's Bank of China (PBoC) and the Ministry of Foreign Affairs in August 2017 (State Council, 2017). Infrastructure connectivity—which includes economic corridors; land-based, sea-based and air passages; information highways; and grand projects in rail, port and pipeline networks—is the core and fundamental part of the BRI.

Geographically, the Belt consists of the northern route of China–Central Asia–Russia–Europe (the Baltic Sea); the middle route of China–Central Asia–West Asia (Middle East)–Persian Gulf and the Mediterranean; and the southern route of China–South Asia and Southeast Asia–Indian Ocean. The Road includes the route of China–South China Sea–Indian Ocean–Europe and the route via the South China Sea to the South Pacific Region (see **Figure 1**).

Table 1. China's investments and construction contracts in BRI countries by sector, 2014–2018

	Sector	Value (US$ billion)
1	Energy	225.48
2	Transport	156.44
3	Real estate	59.76
4	Metals	37.72
5	Others	19.45
6	Utilities	15.24
7	Agriculture	13.5
8	Logistics	12.92
9	Technology	11.18
10	Chemical	10.06
11	Finance	8.55
12	Entertainment	8.49
13	Tourism	7.34
14	Health	2.72
	All sectors	588.85

Data source: American Enterprise Institute (AEI) and Heritage Foundation (2019)

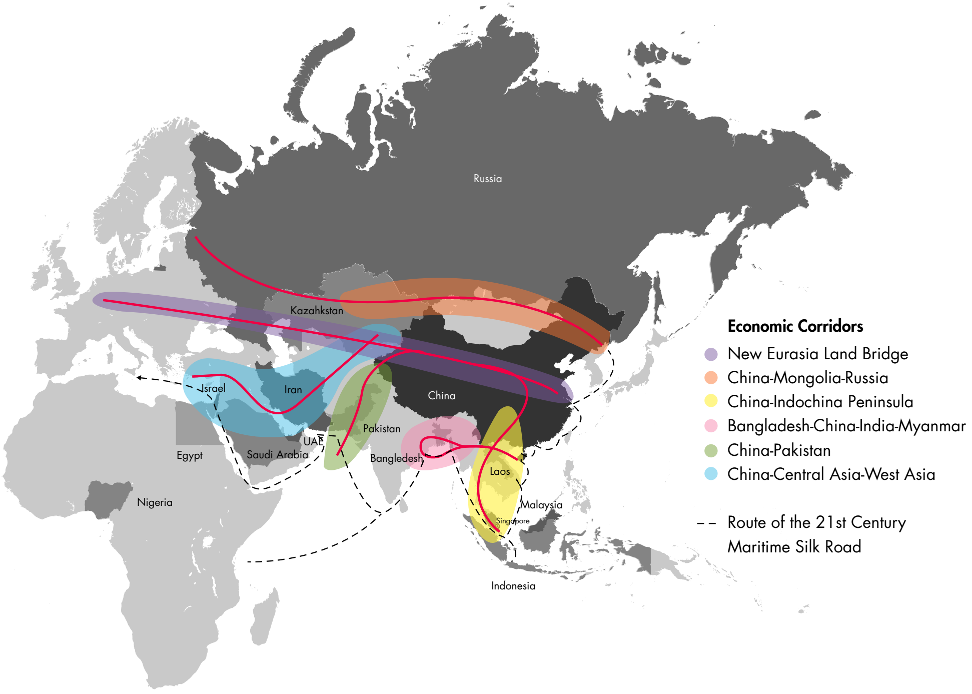


Source: Author/CIGI

Figure 1. Routes of the BRI

Judging by the developments in the first five years of the BRI, the priority regions for infrastructure connectivity are located along six economic cooperation corridors in Southeast Asia, Central Asia and South Asia. They include the China-Pakistan economic corridor; Bangladesh-China-India-Myanmar; the Eurasian Land Bridge; China-Mongolia-Russia; China-Central Asia-West Asia; and the China-Indochina Peninsula (see **Figure 2**), as well as some key railways and ports connecting countries alongside the 21st Century Maritime Silk Road.

Statistics shows that Pakistan, Malaysia, Singapore, Indonesia, Bangladesh, Laos, Israel, the United Arab Emirates (UAE), Egypt and Nigeria are the top 10 countries in which China's total value of investments and construction contracts increased greatly between 2014 and 2018, compared with the eight years (2005–2013) before the BRI was established (see **Tables 2** and **3**). Nine of the 10 countries are all located within the six economic cooperation corridors. In Pakistan, the total number of China's investments and construction contracts tripled in the first five years of the BRI, compared with the previous eight years, and the absolute number of China's total investments and construction contracts in Pakistan is at the top among all other countries along the Belt and Road. In Malaysia, Laos, Singapore and the UAE, the total number of China's investments and construction contracts almost doubled or more than doubled, and in Indonesia, the number increased by 57 percent. The biggest surge happened in Bangladesh and Israel, where the number of China's investments and construction contracts increased six times or almost six times, as the base number in the two countries in 2005–2013 were small. Russia and Kazakhstan are regarded as priority countries, although the total value of China's investments and construction contracts did not increase significantly or even decreased remarkably there, compared with the numbers of the previous eight years. This is because China had already invested heavily in Russia and Kazakhstan before the BRI began in 2013.



Source: Author/CIGI

Figure 2. The BRI's six economic corridors and 14 priority countries

Table 2. China's construction contracts and ODI—Top 10 BRI countries, 2014–2018 (US$ billion)

Country	Contract Value	Country	ODI Value
Pakistan	31.41	Singapore	24.27
Nigeria	24.21	Malaysia	14.09
Bangladesh	17.54	Russia	10.44
Indonesia	16.77	Indonesia	9.35
Malaysia	15.8	Israel	7.88
Egypt	14.95	Pakistan	7.63
UAE	14.03	Laos	6.68
Russia	11.13	UAE	6.55
Laos	11.06	Nigeria	6.54
Iran	10.63	Bangladesh	5.3

Data source: AEI and Heritage Foundation (2019)

Table 3. China's investments and construction contracts before (2005–2013) and after (2014–2018) the BRI—Top 15 countries (US$ billion)

Before		Value	After	Value
1	Russia	22.93	Pakistan	39.51
2	Kazakhstan	22.19	Nigeria	30.75
3	Saudi Arabia	21.56	Malaysia	29.89
4	Nigeria	19.21	Singapore	28.03
5	Indonesia	16.6	Indonesia	26.12
6	Ethiopia	16.57	Russia	24.25
7	Vietnam	16.49	Bangladesh	22.84
8	India	16.17	UAE	21.22
9	Malaysia	15.77	Laos	17.86
10	Angola	14.92	Israel	16.67
11	Iraq	14.71	Egypt	15.69
12	Iran	12.97	Saudi Arabia	13.83
13	Pakistan	12.44	Iran	12.97
14	Singapore	11.51	India	10.93
15	Turkey	10.85	Kazakhstan	10.44

Data source: AEI and Heritage Foundation (2019)

Several symbolic projects in these priority regions and countries were mentioned by President Xi in his speech at the first BRF: Karakoram Highway through the China-Pakistan corridor; Jakarta–Bandung High Speed Rail, China–Laos Railway and China–Thailand Railway down the China-Indochina Peninsula economic corridor; Gwadar Port, Port of Piraeus and Hambantota Port, and Mombasa-Nairobi Standard Gauge Railway and Addis Ababa–Djibouti Railway, connecting countries in eastern Africa and the Indo-Pacific region and Mediterranean region across the 21st

Century Maritime Silk Road; and the Trans-Eurasia Railway (operated by Trans-Eurasia Logistics) and the Hungary–Serbia Railway that constitute part of the Eurasian Land Bridge. Railway and port projects seemed to be the top priority by sector in the first five years.

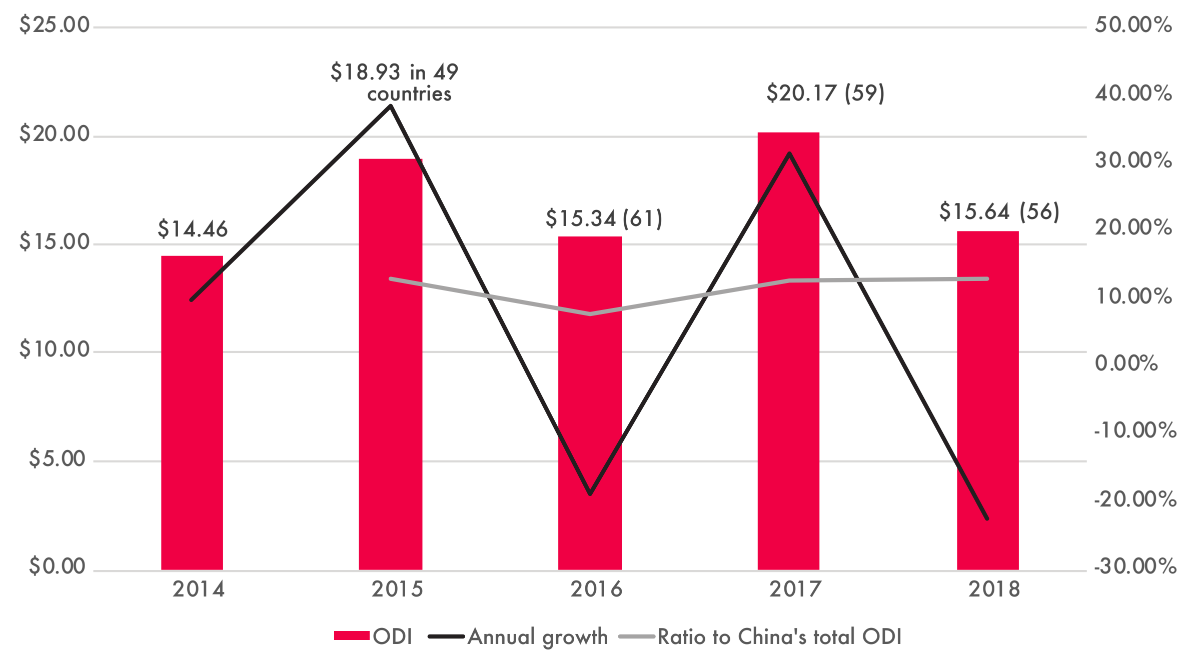
3.2. Achievements

Outward direct investment (ODI) and construction contracts are the two major forms of China's investments in the BRI countries. The value of China's total investments and construction contracts in BRI countries during 2014–2018 amounts to $573.31 billion (see **Table 4**).[3] Both ODI and construction contracts experienced a rapid increase in the first five years of the BRI (see **Figure 3**).[4]

Table 4. China's total BRI investments and construction contracts (2014–2018, US$ billion)

Investment (ODI)	84.54	190.23
Construction contracts	488.77 (2015–2018)	387.69
Accomplished turnover	320.1	N/A
Total (ODI and contract value)	**573.31**	**577.92**
	Data from MOFCOM	Data from AEI

Data sources: MOFCOM (2014; 2015; 2016; 2017; 2018) and AEI and the Heritage Foundation (2019)



Data source: MOFCOM (2014; 2015; 2016; 2017; 2018)

Figure 3. China's ODI in BRI countries (US$ billion).

[3] All dollar amounts are in US dollars unless otherwise stated.

[4] A possible explanation for the drop in both ODI and construction contracts in 2016 and 2018 is that the state-owned enterprises (SOEs) held their investment and contracts until 2017, the year in which the first BRI summit convened, to claim merit for themselves and please President Xi.

China's ODI stock in BRI countries in 2014–2018 accounted for half of China's total ODI stock in these countries as of 2017 (see **Figure 4**). This indicates that China's ODI in BRI countries since 2014 is quite significant in both amount and growth rate. Most of China's ODI went to priority countries along the Belt and Road, such as Indonesia, Malaysia, Russia and Singapore (see **Tables 2**, **5** and **6**). Southeast Asia remains the region that received most of China's ODI among the BRI countries. Singapore has been the country that received most of China's ODI either in flow or stock among all BRI countries, and leasing and business service is the sector that attracted most of the BRI investment in this country.[5] This can be explained by the fact that Singapore mainly acted as a transfer station from where a large number of these investments went to other countries. Even excluding the part of transferred investment, Singapore still attracted the largest amount of Chinese ODI in BRI countries between 2014 and 2018 (see **Table 2**), and most of this part of ODI in Singapore went to sectors in logistics, online shopping, technology, finance and real estate (American Enterprise Institute (AEI) and Heritage Foundation, 2019). China's ODI increased at the fastest growth rate in Malaysia (see **Tables 2, 5** and **6**).

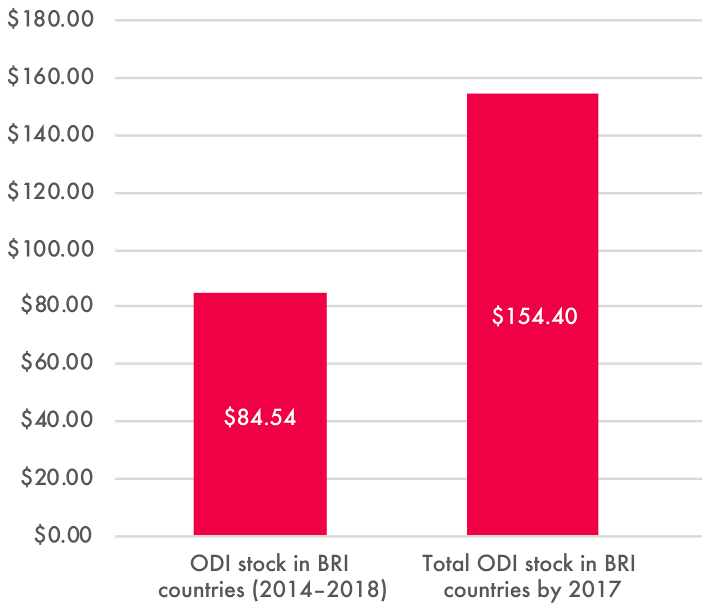
China's construction contracts in BRI countries tell a different story. Pakistan, Nigeria, Bangladesh, Indonesia and Malaysia are the top five countries for Chinese construction contracts; Pakistan, as the top-priority country of China's BRI, is unsurprisingly the country that received the greatest value of China's construction contracts (see **Table 2**).

In China's official narrative, the BRI made great achievements in the first five years after it was initiated in 2013. China's ODI in BRI countries totaled \$84.54 billion in 2014–2018. Rapid growth was achieved in construction contracts in terms of numbers of contracts, value of contracts and accomplished turnover (see **Figure 5** and **Table 5**). The total value of China's construction contracts in BRI counties amounted to \$488.77 billion in 2015–2018 (see **Table 4**). Trade is another aspect of these achievements: newly added volume of trade in goods between China and BRI countries in 2014–2018 was more than \$5 trillion, with an annual growth of one percent. The number of jobs created in BRI countries by June 2018 was 244,000 (State Council Information Office, 2018). Two typical cases highlight this type of achievement: the Mombasa–Nairobi Standard Gauge Railway project with the investment by China Communications Construction Company created 37,000 jobs, and China National Petroleum Corporation-owned Aktobe Oil Company in Kazakhstan hired more than 30,000 local people and accounts for 70 percent of local tax revenue. China's investments have generated \$2.01 billion of tax revenue for the BRI countries (State Council Information Office, 2017).

Beyond the official data, the huge investments in BRI infrastructure projects created great opportunities for Chinese industries in the transportation, energy, hydro, telecommunication and manufacturing sector. In the name of international capacity cooperation, these industrial sectors, led by large state-owned enterprises (SOEs) in each sector, expanded into countries alongside the Belt and Road.

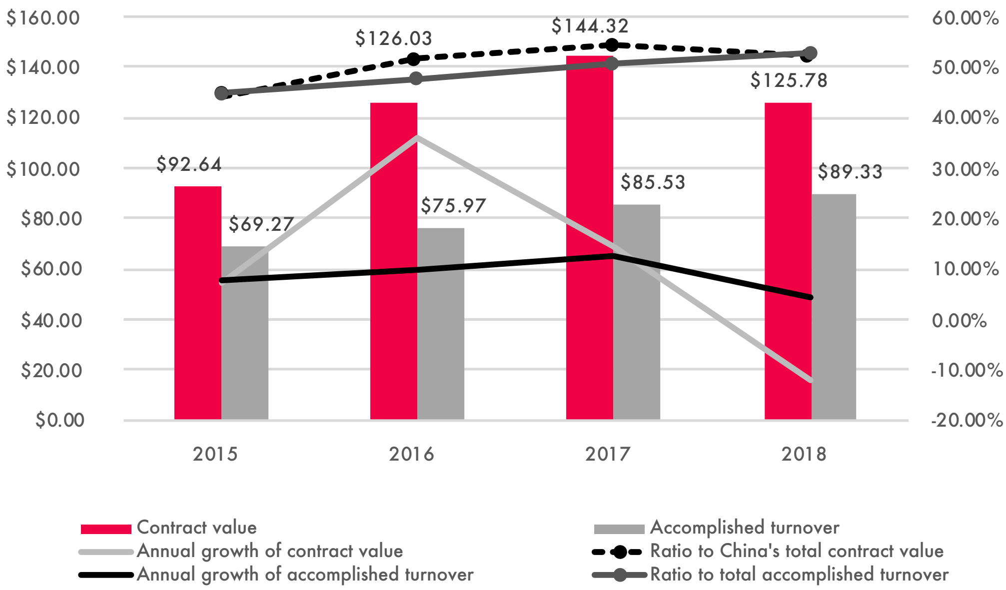
As shown in the 13th Five-Year Plan in 2015, the BRI was defined as the leading project in China's new phase of foreign economic policy, and international cooperation on capacity and

[5] See MOFCOM (2014; 2015; 2016; 2017; 2018). Hong Kong, rather than Singapore, received the most of China's ODI either in flow or stock. However, Hong Kong is not a country and is not included in the statistics on China's ODI on the BRI countries in the MOFCOM reports.



Data source: MOFCOM (2014; 2015; 2016; 2017; 2018)

Figure 4. ODI stock before and after BRI inception (US$ billion).



Data source: MOFCOM (2014; 2015; 2016; 2017; 2018)

Figure 5. China's construction contracts (US$ billion).

Table 5. China's ODI in top 10 BRI countries by year

2017			2016		2015	
Country		US$ million	Country	US$ million	Country	US$ million
1	Singapore	6,320	Singapore	3,710	Singapore	10,450
2	Kazakhstan	2,070	Israel	1,840	Russia	2,960
3	Malaysia	1,720	Malaysia	1,830	Indonesia	1,450
4	Indonesia	1,680	Indonesia	1,460	UAE	1,270
5	Russia	1,550	Russia	1,290	India	710
6	Laos	1,220	Vietnam	1,280	Turkey	630
7	Thailand	1,060	Thailand	1,120	Vietnam	560
8	Vietnam	760	Pakistan	630	Laos	520
9	Cambodia	740	Cambodia	630	Malaysia	490
10	Pakistan	680	Kazakhstan	490	Cambodia	420

Data source: MOFCOM (2016; 2017; 2018)

Table 6. China's ODI stock—Top 10 BRI countries as of 2017

Country		US$ billion
1	Singapore	44.57
2	Russia	13.87
3	Indonesia	10.53
4	Kazakhstan	7.57
5	Laos	6.65
6	Pakistan	4.97
7	Myanmar	5.52
8	Cambodia	5.45
9	UAE	5.37
10	Thailand	5.36

Data source: MOFCOM (2014; 2015; 2016; 2017; 2018)

equipment manufacturing was listed as one of the four development strategies in the new all-around economic opening-up master plan. The Five-Year Plan specifically lists the priority sectors for international cooperation on capacity and equipment manufacturing, including steel, nonferrous metal, building materials, railway, electricity, chemical, textiles, autos, telecommunication, engineering machinery, shipping, aerospace and ocean engineering. Most of these are sectors with overcapacity. The plan also listed the ways for capacity cooperation, including direct investment, contract construction, technological cooperation and equipment export. Both the sectors and ways of cooperation listed in the plan basically coincide with the ones in the BRI; however, the emphasis of the BRI in the Five-Year Plan is specifically given to the cooperation on energy and resources and value chains.

Xi described industrial cooperation as the fundamental way for economic cooperation between China and countries through the Belt and Road, and stressed international cooperation on capacity and equipment manufacturing at the first BRF in May 2017. By that point, China had engaged more than 30 countries in institutionalized capacity cooperation (Xinhua, 2017a). China-Kazakhstan capacity cooperation and the China-Belarus Industrial Park represented two flagship projects in international industrial capacity cooperation.

China's industries with overcapacity, such as steel, coal, metal and hydro, benefit greatly from international capacity cooperation under the framework of the BRI, as the majority of the BRI investments and contracts went to the energy and transport sectors. In the MoU between China and Kazakhstan on strengthening capacity and investment cooperation in March 2015, the agreement on capacity cooperation in steel, hydro, auto, nonferrous metal and flat glass was included. The China-Belarus Industrial Park is an example of China's preferred typical policy to set up a platform for industry agglomeration, in which all sectors can converge and form a scale effect.

The huge demand from the BRI project means that Chinese enterprises in steel and other sectors related to transport are in a prime position (Balhuizen, 2017). Analysts in China's steel sector predicted in 2017 that the demand for steel products in regions along the Belt and Road, in particular in countries in Southeast Asia and the Middle East, would be huge. As a priority sector, capacity cooperation would provide a room for structural reform in the domestic steel sector (Wang, 2017). The BRI will expand overseas markets for China's steel sector and enhance China's status in the value chain for steel (Liu, 2019).

3.3. The BRI as the "Going Out" Strategy 2.0

When the BRI began to get into full swing in 2015, China's "going-out" strategy had been carried out for a decade. There is obvious consistency between the going-out strategy and the BRI as they both focused a great amount of China's overseas outward investments and construction contracts on infrastructure, especially in the transportation and energy sectors. Statistics show this consistency. A large percentage of contracts and investments goes to countries with many previously existing projects, including countries in South and Central Asia such as Pakistan and Kazakhstan; Southeast Asian countries such as Indonesia and Malaysia; East African countries such as Kenya, Ethiopia, Tanzania and Zambia; and Nigeria in West Africa. For the SOEs that dominated China's outward investments and construction contracts in both the going-out strategy and the BRI, increasing their investments in these regions and countries where the going-out strategy and the BRI overlap is convenient. It is beneficial and advantageous for them to do so to show the government that they made noticeable progress for Xi's signature foreign policy initiative in a short period.

Following the same model as the going-out strategy, the principal enterprises that carried out projects of the BRI are the central-government-owned giant SOEs in key sectors such as transportation, energy and telecommunication. In the first three years of the BRI, 47 central-government-owned enterprises participated in 1,767 projects by May 2017 (State Council Information Office, 2017). These SOEs dominate investments and construction contracts in the BRI countries. By April 2019, there were more than 80 central SOEs (Yuan, 2019) participating in the 3,120 BRI projects, accounting for more than 60 percent of total projects and close to 80 percent of total project value (Wang, 2019; Dong, 2019). This means the projects and project value by the private sector are about 40 percent and 20 percent, respectively. According to the statistics by the

AEI, the private share of investment in the BRI reached 49 percent by 2017, an increase from 28 percent in 2014, 17 percent in 2015 and 28 percent in 2016 (AEI and Heritage Foundation, 2019).

The financial support the SOEs received from CDB, one of two major policy banks to provide loans to the BRI, offers a clue to the SOEs' dominance in BRI investments and construction contracts: in 2017, CDB provided $13.4 billion in BRI loans to SOEs out of its total BRI loans of $17.6 billion (CDB, 2017). This is in line with the assumption that only a small portion of China's financing for the BRI went to the private sector.

A few large private enterprises participated in the investment in BRI infrastructure projects, including Huawei, e-commerce and internet giants such as Alibaba and Tencent, auto manufacturer Geely, consumer electronics company TCL and heavy equipment manufacturer Sany Heavy Industry. Some large real estate companies have begun to invest in Southeast Asian countries in recent years. SOEs' huge investments in infrastructure created opportunities for the Chinese private sector to engage in trade and economic cooperation between China and countries along the Belt and Road.

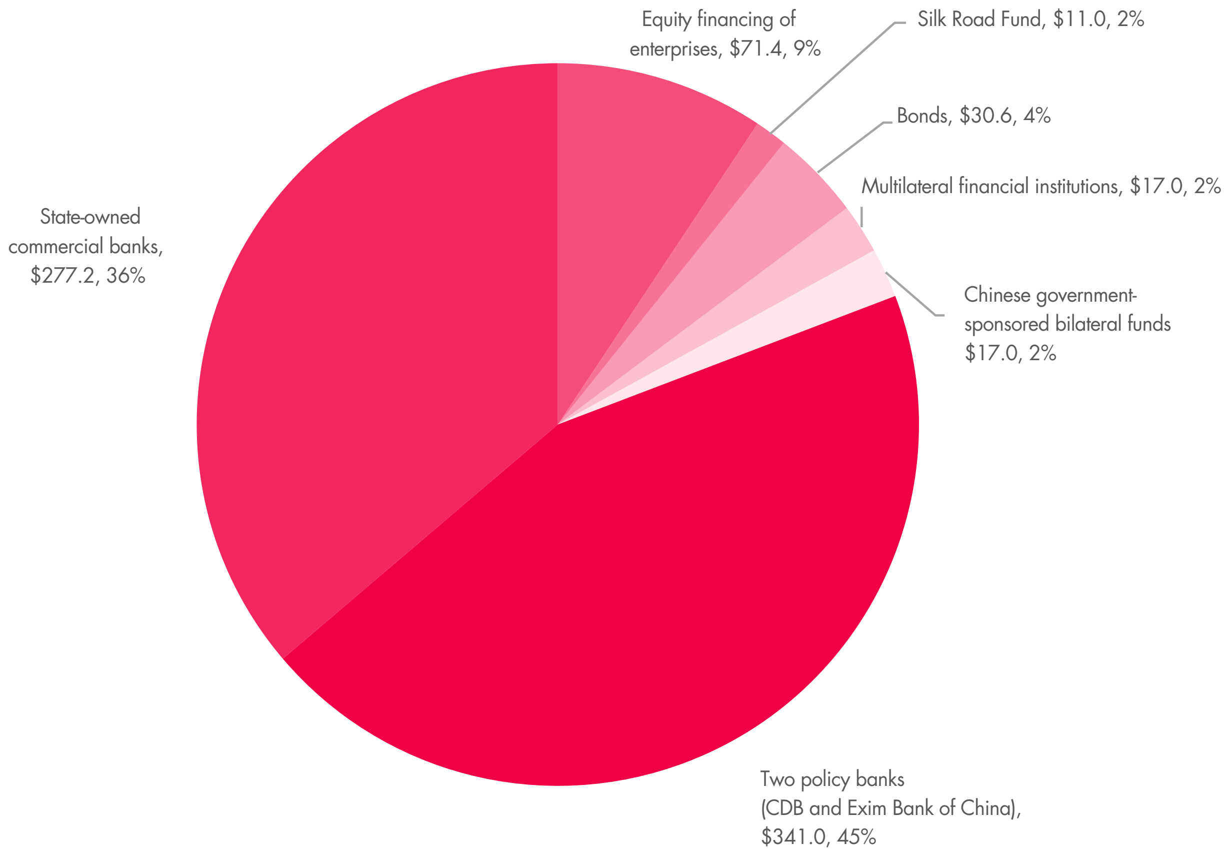
The private sector is increasingly getting involved in the BRI by investing in trade and economic cooperation with countries along the Belt and Road. This constitutes the mainstream way for the private sector's investment in the BRI. Private enterprises dominated most of the China-led overseas industrial parks for economic and trade cooperation along the Belt and Road (Ma and Zhang, 2019). Trade volume by the private sector accounts for 43 percent of China's total trade volume with countries along the Belt and Road in 2017 (Dong, 2019). Among China's top 500 private enterprises, more than half of them (274) had participated in the BRI by 2017 (Dong, 2019).

4. BRI financing

4.1. Financing from China's state-owned banks

China's state-owned policy banks and state-owned commercial banks are the major sources of BRI financing. They account for the majority of BRI funding, providing 81 percent of total BRI funding (see **Figure 6**). They are also the major capital providers for the Chinese government-sponsored bilateral funds and the major issuers of the BRI bonds. Including the six percent provided by the government-sponsored bilateral funds (two percent) and the BRI bonds (four percent), Chinese state-owned banks account for about 87 percent of total BRI funding (see **Figure 6**). The other 13 percent of BRI funding is supported by enterprises' equity financing in Chinese capital markets (nine percent), multilateral financial institutions (two percent)[6] and the Silk Road Fund (two percent) (see **Figures 6** and **7**).

[6] The AIIB and the New Development Bank (NDB) are not exclusively focusing on BRI funding. The loans they provided for projects in the BRI countries are counted as part of the total amount of the BRI funding in the paper.



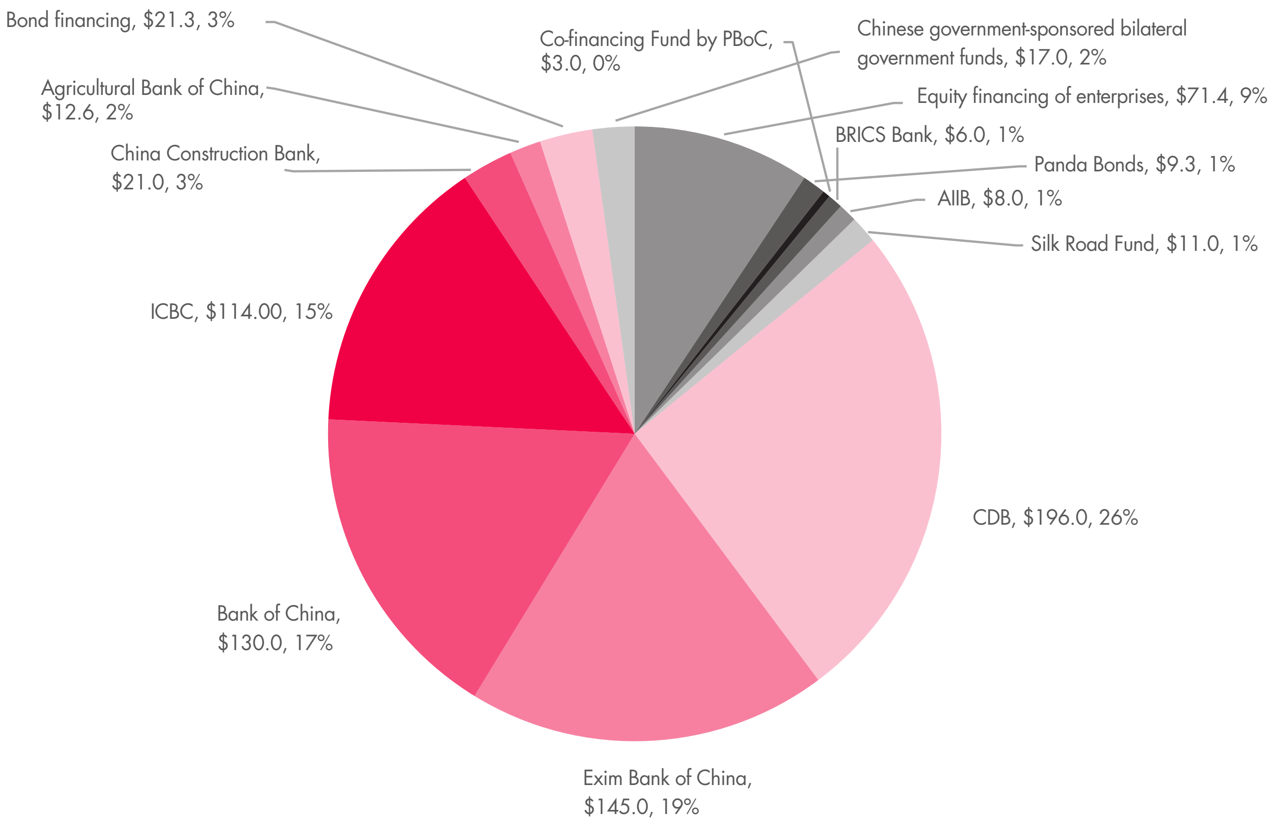
Data sources: The State Council Information Office of China, www.scio.gov.cn; CDB (2017; 2018); Xinhua, www.xinhuanet.com/fortune, www.xinhuanet.com/money; Bank of China (2018); ICBC (2017; 2018); www.ccb.com; https://finance.sina.com.cn/money/bank; www.china-asean-fund.com, www.china-ceefund.com; www.china-eurasian-fund.com; www.sinoceef.com; 21st Century Business Herald, https://m.21jingji.com; Belt and Road Energy Cooperation, http://obor.nea.gov.cn; Russia-China Investment Fund, https://cn.investinrussia.com; MOFCOM, www.mofcom.gov.cn; China-LAC Cooperation Fund, www.clacfund.com.cn; www.the paper.cn; yicai.com; Shanghai Securities News (2019); AIIB (2019); NDB (2018); PBoC (2019); Economic Information Daily, www.jjckb.cn; Climate Bonds Initiative, https://cn.climatebonds.net; www.eximbank.gov.cn;[7] www.ce.cn;and https://zaobao.com

Note: The number of Chinese government-sponsored bilateral funds is estimated. To avoid double counting, the renminbi overseas funds for the BRI are excluded from the figure as the major issuers of these funds are Chinese financial institutions listed here, and the renminbi overseas funds are already included in the numbers by these financial institutions.

Figure 6. BRI funding by source type at the end of 2018 (US$ billion).

Two large state-owned policy banks, the CDB and Exim Bank of China, are the main sources of BRI financing, accounting for 45 percent of the total. Of the two, the CDB is the largest funding source for the BRI and had provided about $196 billion in loans by the end of 2018, accounting for 26 percent of the total amount of the BRI financing (see **Figure 7**). Exim Bank supplied more than $145 billion on 1,800 projects by the same year-end, representing 19 percent of the total amount of BRI financing (see **Figure 7**).

[7] Calculated based on the news release on the website of Exim Bank of China: www.eximbank.gov.cn/tm/m-newinfo/index.aspx?nodeid=454&contentid=30527; www.eximbank.gov.cn/tm/Newlist/index_343_30615.html.



Data sources: Ibid
Note: The number of Chinese-sponsored bilateral government funds is estimated

Figure 7. BRI funding by source at the end of 2018 (US$ billion).

Four big state-owned commercial banks, the ICBC, Bank of China, the China Construction Bank (CCB) and the Agricultural Bank of China constitute another significant source for BRI financing. They provided a total of $227.2 billion by year-end 2018. Among them, Bank of China and the ICBC provided most of the credit lines. By the end of 2018, Bank of China provided a total of $130 billion in credit line support on 600 projects, ICBC provided $114 billion on 441 projects and CCB signed loan agreements worth $20.6 billion on 29 projects in 29 countries. The Agricultural Bank of China helped Chinese enterprise financing in the form of issuing loans and insuring and issuing bonds overseas, and the total amount of financing it provided for investments in BRI countries was $12.6 billion from 2014 until the first half of 2018 (see **Figures 6** and **7**).

4.2. Government-owned investment fund

The Silk Road Fund was established by the Chinese government in 2014 as the state-owned fund exclusively focusing on investments for the BRI. Its total assets are $40 billion, and 65 percent of it was supplied by China's foreign reserve through the investment company Buttonwood Investment Holding Co. Ltd. owned by China's State Administration of Foreign Exchange. China's sovereign wealth fund, China Investment Corporation (CIC), owns 15 percent of the Silk Road Fund through a subsidiary. Exim Bank of China accounts for 15 percent of its ownership and another five percent is owned by the CDB.[8] The Silk Road Fund got an extra RMB100 billion (≈$14.7 billion) capital injection from the Chinese government in May 2017. By the end of 2018, the Silk Road Fund provided $11 billion for 30 projects (see **Figures 6** and **7**).

There are some bilateral and multilateral funds jointly sponsored by the Chinese government and other governments for the BRI. They are essentially jointly funded in name only, however, and China's state-owned banks are usually the major sponsors behind them. Some of them were set up before the BRI was initiated but counted in the initiative after the BRI's inception. Data for the total amount of investment by these funds in BRI projects is difficult to obtain. The author tried to track the major bilateral funds (with a fund size above $1 billion) for the BRI, and the total capital of these funds amounted to $84.6 billion by the end of 2018 (see **Table 7**). Assuming that 20 percent of each fund has already been spent (as the case of the China-Africa Fund for Industrial Cooperation (CAFIC) below shows), the amount invested in BRI projects is about $16.9 billion by the end of 2018. Major funds of this type include the China-ASEAN (Association of Southeast Asian Nations) Investment Cooperation Fund (CAF), the China-Central and Eastern Europe Investment Cooperation Fund (China-CEE Fund), the China-Central and Eastern Europe Fund (Sino-CEEF), the China-Eurasian Economic Cooperation Fund (CEF), the Russia-China Investment Fund (RCIF), the CAFIC, the China-Africa Development Fund (CADF), the China-LAC Cooperation Fund (CLCF), the China-LAC Fund for Industrial Cooperation (CLFIC), the China-United Arab Emirates Joint Investment Fund (CUJIF) and China-Qatar Joint Investment Fund (CQJIF) (see **Table 7**).

Chinese provincial governments also sponsored local Silk Road funds, each with about RMB10 billion. However, the amounts of these funds invested in projects in countries along the Belt and Road are not significant. Only a small portion of the capital from these funds had been invested by 2018. For example, the Guangdong Silk Road Fund, with about RMB20 billion initiated in 2016, had invested in two projects worth RMB4.599 billion by February 2018 (Dai and Chen, 2018). Enterprises' investment funds for the BRI began to emerge in 2015 but usually focused on domestic projects and did not invest in great numbers by year-end 2018. They typically go with a scale of RMB10 billion and a first phase of RMB1 billion. The funding from Chinese provincial governments and enterprises is not counted in the total amount of BRI financing in the paper.

4.3. Financing from multilateral financial institutions

The AIIB and the BRICS (Brazil, Russia, India, China and South Africa) Development Bank (now called the New Development Bank, or the NDB), the two multilateral development banks China initiated were not established to exclusively provide financial support for the BRI. However, most of the projects they provide loans for are in countries and regions along the Belt and Road. The geographical overlapping justifies the inclusion of these multilateral development banks in BRI financing. The AIIB has provided loans and other forms of lending totaling close to $7.5 billion as of the end of 2018 (AIIB, 2019). This amount includes financing for a number of projects outside Asia (AIIB, 2019), but the majority of the loans and lending it has committed are located in countries along the Belt and Road.[9] The NDB's total lending commitment by the end of 2018

[8] See the website of the Silk Road Fund for the shareholder structure: www.silkroadfund.com.cn/enweb/23775/23767/index.html.

[9] Jin Liqun, the president of the AIIB, mentioned that by July 2018, all projects the AIIB invested in were located in countries and regions along the Belt and Road. See Han and Wen (2018).

Table 7. Major bilateral funds for the BRI (US$ billion)

Fund	Fund Size	Phase I	Phase II	Realized Investment by 2018	Year of Initiative	Major Sponsors
CAF	10	1	3	N/A	2009	China Exim Bank, CIC, Bank of China
China-CEE Fund	1.435	0.435	1	N/A	2013	China Exim Bank
Sino-CEEF	€10 ($11.12)			N/A	2016	ICBC
CEF	5	1		N/A	2014	China Exim Bank, Bank of China.
RCIF	2			N/A	2012	RDIF, CIC
CAFIC	10			1.795	2015	Buttonwood, China Exim Bank
CADF	5*	1	2	N/A	2007	CDB
CLCF	10	5	5	N/A	2014	China Exim Bank
CLFIC	10			N/A	2015	Buttonwood, CDB
CUJIF	10	4		N/A	2015	CDB, Mubadala
CQJIF	10			N/A	2014	CITIC, Qatar Investment Authority
Total	84.555			16.911 (estimated)		

Data sources: China-asean-fund.com, obor.nea.gov.cn, China-ceefund.com, 16plus1-thinktank.com,[http://16plus1-thinktank.com/1/20180305/1587.html.] China-eurasian-fund.com, cn.investinrussia.com, 21st Century Business Herald, mofcom.gov.cn, clacfund.com.cn, thepaper.cn and yicai.com
** In 2017, it was announced that another $5 billion would be added to this fund*
Note: The China-Kazakhstan Industrial Cooperation Fund is funded by the Silk Road Fund and is not included here to avoid double counting. The China-Russia Regional Cooperation and Development Fund is excluded here as it was only announced in September 2018 and is not yet operating.

reached approximately $8 billion (NDB, 2018). Of this, the total lending commitment to India, Russia and China, three BRI countries, is $5.98 billion.[11]

The PBoC has cooperated with the African Development Bank, the Inter-American Development Bank and the International Finance Corporation (a member of the World Bank Group) and established co-financing funds with a total worth of $7 billion and contributed €0.25 billion to the Equity Participation Fund of the International Bank for Reconstruction and Development. By the

[10] http://16plus1-thinktank.com/1/20180305/1587.html.

[11] The number is the result of calculations based on the list of all projects on the website of the NDB.

first quarter of 2019, these financing mechanisms had already invested more than $3 billion on nearly 200 projects (PBoC, 2019).

4.4. Bond financing

A number of China's financial institutions and enterprises have issued a few bonds for BRI projects since 2015. But the total amount of the capital via bond financing is still quite small, compared to the loans provided by financial institutions such as CDB and other state-owned commercial banks. Among them, Bank of China topped other institutions and has issued bonds worth a total of close to $15 billion in RMB, Hong Kong dollars, US dollars and euros from 2015 to the end of 2018. Agriculture Bank of China was the first in China's "big four" state-owned commercial banks to issue a green bill. It issued a $1 billion green bill on the London Stock Exchange in October 2015. The total of bonds issued by other banks exclusively on the BRI is relatively smaller. Altogether, bonds issued by China's state-owned banks in the name of the BRI (including green bonds that claimed they would invest in the BRI) totaled about $21.31 billion (calculated based on the number below). If the bonds issued overseas by Exim Bank and the CDB are included, the total is $50.31 billion (see **Table 8**).

Panda bonds issued by countries and companies in the BRI in Chinese capital markets amounted to RMB65 billion (≈$9.3 billion) by April of 2019 (Shanghai Securities News, 2019).

As the main entities that invested in BRI projects, the capital of Chinese SOEs are also important sources for BRI funding. However, the total capital raised by the SOEs themselves and invested in BRI counties is not available. Yi Gang, governor of the PBoC, mentioned in a speech that China's capital market had provided about $71.4 billion for enterprises via equity financing for BRI projects by April 2019 (Shanghai Securities News, 2019).

Table 8. BRI bonds issued by Chinese financial institutions by 2018 (US$ billion)

Issuer	Size	Exclusive BRI Bonds	Green Bonds	Issued Overseas	Time of Issue
Bank of China	15	Y	N/A	Y	2015–2018
CDB	16.4	N	N/A	Y	2015–2018
CDB	1.67	Y	Y	Y	2017
China Exim Bank	11.6	N	N	Y	2015–2018
China Exim Bank	0.3*	Y	Y	N	2017
CCB	0.16**	Y	N	Y	2015
CCB	0.45***	Y	N	Y	2016–2018
ICBC	3.73	Y	Y	Y	2017–2018
Agriculture Bank of China	1	N	Y	Y	2015
Total	**50.31**	**21.31**			

Data sources: Economic Information Daily; Shanghai Securities News, http://news.cnstock.com/; Climate Bonds Initiative; www.eximbank.gov.cn; www.ccb.com; ce.cn; www.xinhuanet.com; www.zaobao.com; and www.abchina.com
** RMB2 billion in November 2017, ** RMB1 billion in November 2015, *** RMB3 billion between 2016 and 2018*

5. Ever-expanding themes of the BRI

The BRI's core idea is to promote economic growth in both China and countries along the Belt and Road through connectivity via land-based and maritime infrastructure, as well as industrial capacity cooperation between China and these countries. By April 2017, when the first BRF was held in Beijing, several themes had been added to the framework of the BRI and demonstrated President Xi's and China's growing ambition in many respects, including the Green Silk Road initiative, the Digital Silk Road, the Polar Silk Road (the Arctic shipping route) and the BRI as the road map to promote Xi's idea of building a community of shared future for mankind. In this sense, the BRI as President Xi's signature foreign policy has evolved into a much more expansive package of national strategies that contains a series of goals in both foreign policy and domestic economic growth.

Among them, the idea of the BRI as China's major initiative to participate in global cooperation is President Xi's favorite. Xi described three components on how the BRI would contribute to global economic cooperation in his opening speech at the first BRF. The first is a new type of international relations of win-win cooperation among BRI countries. The second is economic co-development and prosperity through cooperation in industry, finance and infrastructure connectivity that includes connectivity in policies, rules and standards. The third is maintaining an open world economy through global governance and providing public goods and encouraging free trade and investment in a multilateral trade system.

Xi further defined the BRI as "the great practice for the community of shared future for mankind." He personally confirmed this at the dialogue between the Communist Party of China and leaders of major parties of the world in December 2017 by saying, "I first proposed the BRI to practise the idea of the community of shared future" (Xinhua, 2017b, para. 8). The Party later defined the BRI as the great platform for the practice of the community of shared future for mankind on the fifth anniversary of the BRI in August 2018.

Through these actions, the BRI was solidified as a key component of Xi's vision for global governance. As he put it at the meeting on the fifth anniversary of the BRI in 2018, the BRI is becoming China's approach to participate in global economic cooperation, improve models of global development and global governance, promote healthy economic globalization, and build the community of shared future for mankind (Xinhua, 2018).

Xi did not explain in detail how the BRI can improve global economic governance but has been advocating a principle of achieving shared growth through discussion and collaboration for China's version of global governance. In China's official narrative, the BRI follows the principle and answers the request for reforming the global governance system and highlights the significance of a shared future and shared rights and responsibilities in global governance by emphasizing the promotion of projects with host countries in a consultative, cooperative, win-win way. In his speech at the China-France Forum for Global Governance in March 2019, Xi added that the BRI enhanced the concept of multilateralism and international economic cooperation as it is an important way to promote world economic growth and co-development.

While there has been some focus on Xi's enthusiasm and efforts to describe the BRI as a solution for China's efforts to improve global economic cooperation with a moral high ground, the green

BRI and the digital BRI have attracted more global attention in recent years.

Green and low-carbon developments were mentioned in the BRI road map in 2015. Xi advocated green, low-carbon and sustainable developments at the first BRF opening speech in 2017 and proposed to jointly establish the BRI International Green Development Coalition with the United Nations Environment Programme. The Chinese government issued Guidance on Promoting Green Belt and Road and the Belt and Road Ecological and Environmental Cooperation Plan after the first BRF. The BRI International Green Development Coalition was officially established in 2019 at the second BRF and will act as a platform for policy communication, environmental knowledge sharing and green technology transfer. China's National Green Development Fund and other state-sponsored funds for the BRI, as well as green bonds issued by China's state-owned banks, are encouraged to invest more in green BRI projects.

The rapid development of the digital economy in the last 10 years was officially absorbed into the BRI at the first BRF in 2017. President Xi proposed building the BRI as a road of innovation and the idea of the Digital Silk Road at the BRI summit through "intensify[ing] cooperation in frontier areas such as digital economy, artificial intelligence, nanotechnology and quantum computing, and advanc[ing] the development of big data, cloud computing and smart cities" (Xinhua, 2017a, para. 35). Over the next two years, the NDRC's Center for International Cooperation led the efforts to promote cooperation among BRI countries on the Digital Silk Road. By May 2019, when the second BRI was held, China had already signed MoUs with 16 countries on building the Digital Silk Road (Huang, 2019). China has advantages in internet, wireless internet (5G) and telecommunications technologies, and is providing key digital infrastructures in these sectors. SOEs are setting global standards for technology and equipment through their investments in BRI countries, which is part of what Xi meant by "connectivity in rules and standards" at the first BRF. For instance, State Grid, China's state-owned power company, is actively promoting China's standards at the International Electrotechnical Commission and the Institute of Electrical and Electronics Engineers through its participation in BRI projects.

The idea of the BRI is not bounded by geographic restrictions or limited to the expansion into the Western Hemisphere. It extended into Latin America in 2017, defining the area as a natural extension of the BRI. China had signed MoUs with 19 countries in Latin America by the first half of 2019 (Belt and Road Portal, 2019), including Panama, Chile, Costa Rica and Venezuela. China has also been encouraging Western developed economies to join the BRI since 2015. In March 2019, Italy became the first G7 member to join the BRI. In addition to the crucial land-based and maritime Silk Roads, the Polar Silk Road through the development of the Arctic shipping routes has been raised in the years since 2013. The idea of sector-based Silk Roads, such as an air Silk Road, an energy Silk Road and an electricity Silk Road, were suggested as well by relevant Chinese government agencies and sectors.

In summary, the evolution since 2013 has shown that the BRI is an ever-expanding package of strategies. President Xi has continued to inject new meanings into it to serve his newly emerging moral-high-ground ideas and ambition in global economic governance.

6. Problems and risks facing the BRI

Debt-trap diplomacy has become a common accusation against China's BRI since 2017, when Indian scholar Brahma Chellaney (2017) first linked the BRI with being a debt trap. It has become a buzzword among China bashers in political, business, media and academic circles around the world in the past two years.

However, the allegation that the Chinese government deliberately put countries in the BRI into a debt trap is not based on solid evidence. Academic studies on China's overseas lending by three institutions have provided data that suggests this claim may be inaccurate. The Center for Global Development finds that the "BRI is unlikely to cause a systemic debt problem in the regions of the initiative's focus" (Hurley *et al.*, 2018, p. 5). The data from the China-Africa Research Initiative at Johns Hopkins University shows that non-Chinese lenders still held the majority of the debt in 17 countries that the International Monetary Fund (IMF) identified as in or at risk of "debt distress" (Brautigam, 2019). Based on their studies of China's investments in Latin America and the Caribbean, researchers at the Global Development Policy Center concluded that Chinese loans alone did not cause these countries to go above the IMF's debt-sustainability thresholds. Venezuela is the only exceptional case (Ray and Wang, 2019).

Venezuela, however, is a case that proves that China does not want to put countries in the BRI into a debt crisis.[12] As a result of its unwise decision to invest heavily in Venezuela, China became a victim of its misjudgment and fanciful strategic thinking in making Venezuela the country's major alternative oil supplier in the future. It is reasonable for China to expect Venezuela to resolve the debt crisis and pay China back sooner.

The case of Sri Lanka is often cited to epitomize China's debt-trap diplomacy. However, a close look at China's investment in Sri Lanka tells a different story. The case study of Sri Lanka in Box 1 shows that there are insufficient grounds for the intentional debt-trap allegation against China.

Box 1. Case study of Sri Lanka

The Hambantota Port project is the focus of public opinion on China's debt-trap diplomacy in Sri Lanka. The project began in 2007–2008, six years before the BRI's inception. It was Sri Lanka that took the initiative to ask for financial help from China to support the project in the first place (Zhou, 2019), and China provided the funding with good intentions, while India and multinational development banks turned their backs on the project (Koh, 2018).

China tried to satisfy Sri Lanka's requests for concessional loans. Exim Bank is the only Chinese bank providing concessional loans and preferential export buyer's credit, and it provided most of the concessional loans Sri Lanka received from China. Reports show that Exim Bank of China provided $306 million for Phase One of Hambantota Port, 85 percent of the total cost in 2007, with a fixed rate of 6.3 percent in a 15-year commercial loan agreement. Later, Exim Bank provided $900 million for the second phase with a concessional loan with a two-percent fixed rate (Koh, 2018).

Hambantota Port incurred heavy losses in 2016, making debt repayment difficult. The fundamental reason that underlines the heavy losses is bad judgment or negligence of profitability and the financial sustainability of the project in the years to come. The deficiency in project selection, plus poor governance and the lack of matching commercial and industrial activities around the port, led to its inability to attract passing vessels to dock at the port and caused significant losses ($304 million) between 2010 and 2016 (Koh, 2018). Both the Chinese government as the investor and the Sri Lankan government as the receiver of the investment are to blame for this poor investment.

The Sri Lankan government has offered China Merchants Ports Holdings a public-private partnership deal that puts Hambantota Port under a 99-year concession lease. China Merchants invested $1.12 billion to revive the port under the deal and to take charge of developing and operating the port.

Sri Lanka's debt to China was about $4.6 billion, accounting for only 10 percent of the $46.5-billion total external debt of this country at the end of 2016, according to the IMF (2018). Data from the annual reports of the Central Bank of Sri Lanka showed that outstanding Chinese loans made up about 9.2 percent at the end of 2017 and 9.1 percent at the end of 2018 of Sri Lanka's total external debt (Central Bank of Sri Lanka, 2017; 2018).13 About 61.5 percent of China's loans to Sri Lanka were concessional loans at the end of 2017 (Daily FT, 2018). This number is 16.5 percent higher than 45 percent, the percentage of Sri Lanka's concessional loans to its total external debt (MOFCOM and the Chinese Embassy in Sri Lanka, 2018).

China's involvement in Hambantota Port demonstrated a deeply rooted problem in China's model of investment: political consideration prevails over economic calculation, which brought great hidden risks and problems of losing money and being "white elephant" projects, thus intensifying debt distress in receiving countries. Chinese loans only account for 10 percent of Sri Lanka's total external debt. However, for Sri Lanka, a small economy that is already heavily indebted, China's huge amount of investment over a short period nonetheless would push it to the brink of a debt crisis.

In any case, the fact that China took over Hambantota Port under a 99-year concession lease has already had a significant negative impact on how the intention behind China's huge investment in Sri Lanka is viewed. Although the new investment by China Merchants helped mitigate the debt problems of the port and is keeping it alive and growing, a lack of transparency in the project proposal, decision making, project bidding and financing contributed to this twisted perception of China's intention for its investment in Hambantota Port. An important lesson China should learn is how to take steps to improve transparency, as China does not participate in certain conventions, such as the Paris Club, that intend to inform creditors and avoid over-lending.

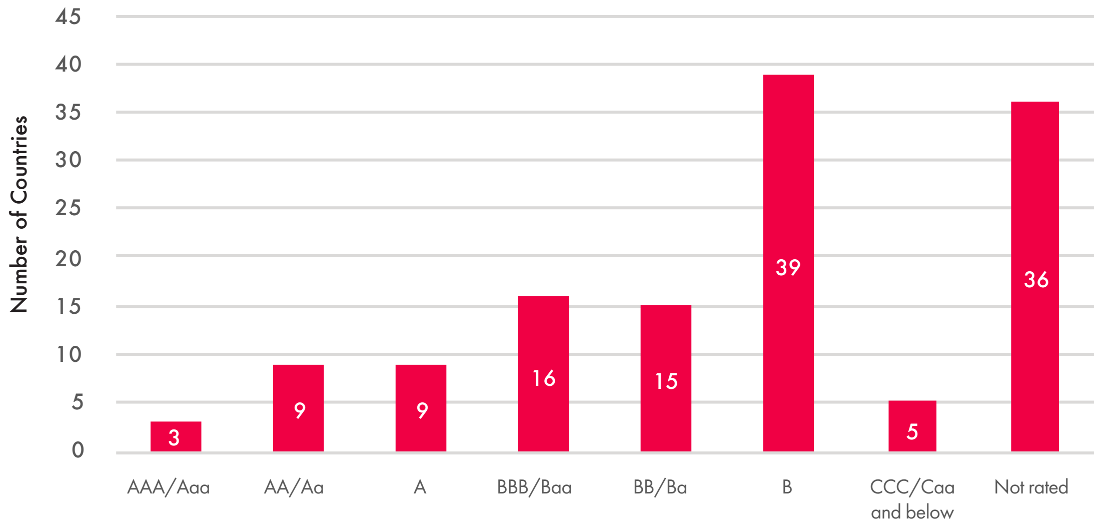
The debt-trap accusation fails to understand the essential part of why China's investments in BRI projects caused debt distress, as it is based on a misreading of China's BRI. The problems and risks in BRI projects originated in China's long-established overseas investment model, in which the NDRC takes charge of project approval, the central government-owned SOEs are responsible for implementing projects and state-owned policy banks and commercial banks provide financial support. Most of the investments usually go to huge projects on transport, energy and other resources, and the Chinese government provides high-level policy communication with the governments in receiving countries to smooth the process of investment. This model is inherited from China's long-standing domestic practices of state-driven investment. It is basically an upper-level route instead of a grassroots-level, market-oriented way of investment, which typically can lead to many problems and risks, including non-transparency, corruption, lower economic efficiency, a lower degree of localization and the lack of participation by the private sector and international investors.

The lack of transparency in bidding, financing and effective dispute settlement are the problems that are immediately generated by the state-driven investment model. Projects that follow this model will certainly experience local dissatisfaction and resistance because of wide criticisms on corruption, negligence of environmental sustainability, the lack of local participation and the lack of matched social projects for an inclusive development goal. As the case of Sri Lanka showed, a transparent process of Chinese investment under the BRI could have benefited both the receiving countries and China itself. Being transparent in project selection, bidding and financing is an effective way to avoid over-lending and thus prevent aggravating debt distress in the receiving countries, in particular those that are already heavily indebted. In this way, the receiving countries could avoid unwise large investments, thereby staying away from a debt crisis, and Chinese SOEs and banks could take a more cautious approach and circumvent risky investments that would not profit for years, thus helping to improve the financial sustainability for the BRI as a whole.

Low economic efficiency and debt risks for the Chinese SOEs and state-owned banks that dominated the investments are inherently caused by soft budget constraints and guaranteed government bail-out, the long-existing unsolved problems of SOEs and state-owned banks. As a result, the economic returns and debt sustainability of the investments are not the top priorities for the SOEs and state-owned banks. For officials in the government, SOEs and banks, treating the BRI as a political task is the most important thing, and the unwritten principle for BRI decision making and implementing involves political considerations. In other words, the essential goal for these officials is pleasing China's paramount leader with their records of contribution to the BRI and increasing their chances for promotion.

An unfavorable investment environment in most of the BRI countries further put China's investments in a disadvantageous position, with a higher political and economic costs and thus exacerbating the problems of low economic efficiency and debt unsustainability. Low sovereign credit ratings, poor performance in domestic governance and an unstable political environment underline the adverse investment environment in most of the BRI countries. The majority of the BRI countries have a sovereign credit rating of highly speculative grade, non-investment grade and lower-medium grade, ranging from B to triple B categories (see **Figure 8**). These countries run a high risk of default. To make it worse, Chinese banks did not show a convincing record that they have adequate capacity to identify profitable projects and manage risks. For the purpose of winning contracts when facing competition from other international investors, Chinese investors would drop some necessary requirements, which added extra risks to Chinese investments. For example, Chinese enterprises gave up the protection of government guarantee from the receiving countries for their investments in high-speed rail projects in Malaysia, Thailand and Indonesia in order to win contracts over highly competitive Japanese companies.

Figure 8. Sovereign credit ratings for BRI countries.



Data sources: Trading Economics, https://tradingeconomics.com/country-list/rating; www.yidaiyilu.gov.cn
Note: The ratings are from Standard & Poor's, Moody's and Fitch, based on the data from Trading Economics. The figure here includes 132 countries. For each country, the highest rating from any of the three rating agencies is used. The 131 countries that signed documents for cooperation with China on the BRI are counted in here. Israel is counted, although there are no official cooperative documents signed between China and Israel on the BRI.

The majority of projects are invested by SOEs and financed by state-owned banks, which makes the BRI appear to be an official aid from China and explains the weak or infrequent participation of the private sector and the small portion of funding from international development financing institutions.

The asymmetric structure between the size of China's huge economy and the smaller economies in most of the receiving countries along the BRI makes the latter vulnerable to problems such as debt distress. Plus, the rapid growth of China's investments in BRI projects over a short period of time further intensified the accumulation of debt problems. Some receiving countries, such as Malaysia and Sri Lanka, simply could not absorb the huge amount of Chinese loans and investments over a short span of time, which led to debt problems.

7. Conclusion: The future of the BRI

China's interactions with recipient countries and its response to critical opinions have a significant impact on the future advancement of the BRI. The accusation of debt-trap diplomacy, although it is not based on solid proof, has contributed to serious concerns over debt sustainability in BRI countries around the world. China has denied that it has ever intentionally set a debt trap in any of the BRI countries, and there is no evidence to prove it did so. The Sri Lanka case study showed that the Chinese did not use debt-trap diplomacy to get control of Hambantota Port.

However, debt sustainability remains a crucial problem in China's investments in BRI projects. The debt problem exists widely in developing countries in their endeavor for a stable and sustainable economic growth. The huge amount of Chinese investments in a short period of time did increase the risk for debt distress in some of the BRI countries, including, but not limited to, Sri Lanka, Malaysia, Cambodia, Bangladesh, Nepal, Indonesia, the Maldives, Pakistan, Ethiopia and Kenya, where China invested a lot under the BRI. These countries generally do not have many options when provided with a large sum of Chinese capital as their governments have long been preoccupied with serious economic, political, social and environmental problems. If China failed to pay enough attention to the problem of debt sustainability when investing in large projects, its huge amount of investments could push these countries closer to the brink of a debt crisis.

China has realized the importance of debt sustainability and responded with measures to improve it in the receiving countries. As one of the key measures to mitigate the debt risks, the MoF, based on the analysis by the IMF and the World Bank on the debt sustainability of low-income economies, has worked on developing the Debt Sustainability Framework for Participating Countries of the BRI since 2017 and eventually released it in April 2019. Together with the cooperation of its counterparts from 28 partner countries, China tried to improve the quality of decision making concerning investment and financing, as well as debt management for a high-quality, high-standard and sustainable system for financing. The MoF led the establishment of the Multilateral Cooperation Center for Development Financing as well, together with eight multilateral development banks and financial institutions. As a coordination mechanism, the Center is expected to improve project financing through information sharing, project preparation and capacity building.

Seen from a domestic perspective, China's financial sustainability for the BRI has emerged as the fundamental concern among all the problems and risks facing the BRI. Apparently, the model for Chinese investment in BRI projects, which relies heavily on government financing, faces great challenges in keeping the initiative financially sustainable. Among these challenges, the low economic efficiency and debt risks facing Chinese SOEs and state-owned banks that invested heavily in the BRI countries pose potentially the greatest risk to financial sustainability. If things continue this way, low economic efficiency would hurt China's capacity for BRI financing, which is highly dependent on loans from the CDB and Exim Bank of China, as well as other state-owned commercial banks. China's foreign reserves are important sources of capital in the CDB and Exim Bank, and the decline of foreign reserves in recent years indicates the unsustainability facing the current model of BRI financing.

Domestic constraints on financing and investment, together with criticisms on debt sustainability from both outside and within China, will push China to seek cooperation with foreign companies, international organizations and foreign capital and substantial support from multilateral financial institutions to sustain BRI projects in the coming years. This has the potential to create win-win cooperation on the BRI between China and other developed economies.

Diversifying the means of BRI financing for stable and sustainable financing arrangements has been under way in recent years. China's capital market has provided about $71.4 billion for enterprises via equity financing, and panda bonds in China's capital market issued by countries and enterprises along the Belt and Road amount to $9.3 billion (Shanghai Securities News, 2019). But still, the majority of BRI financing is provided by China's state-owned policy and commercial banks.

The ever-expanding themes for the BRI have already attracted strong suspicion from the United

States and most of its major Western allies on China's geopolitical and geo-economical strategies to reshape the world economic and political order. China continues to deny that its geopolitical strategy is to overthrow the existing global economic and political order. The advancement of the BRI, with its huge investments, however, will certainly allow China to have profound impacts on the current global economic order by setting the rules and standards in infrastructure and many other sectors and providing public goods to countries along the Belt and Road.

Furthermore, defining the BRI as the road map for building a community of a shared future for mankind, Xi's idea on global governance, has strengthened this suspicion instead of easing it. In any case, the BRI represents an alternative model for development across the world, a path of state-driven investment and development. The BRI constitutes China's idea and practices to promote world economic growth through state-dominated investments in infrastructure connectivity and trade promotion, which is different from the Western or American way of liberal democracy and free-market economy. In the eyes of the Western established powers, the state-driven model of development China provided to advance the economic growth in emerging markets and underdeveloped economies should be scrutinized carefully for its potential risks and problems.

The real challenge to China's measures to improve debt sustainability lies in whether China would make the BRI a true multilateral arrangement. China has opaquely been advocating the principle of achieving shared growth through discussion and collaboration on China's investments in BRI projects. Basically, the principle means China would welcome the involvement of multilateral institutions and other relevant countries and would share the decision making with them through discussion and consensus. But China would not cede control of the final say to the multilateral institutions or the receiving countries on decision making in terms of BRI projects. In China's view, the BRI is a China-dominated multilateral network that is based on bilateral cooperation between China and other receiving countries. In this respect, the best-case scenario would be the AIIB, which provides a good example of China's cooperation with international organizations and other countries in financing the BRI projects. China initiated the AIIB and has remained the largest donor; the AIIB has developed a good reputation as a high-standard multilateral development institution.

The BRI is, however, not the AIIB. Whether China's measures to mitigate debt distress and improve debt sustainability for BRI projects would make any difference remains to be seen. The key issue is how much China can change its state-driven model of investment in the BRI—i.e., how serious the promises by China are on mitigating debt distress and improving debt sustainability for BRI projects, and perhaps most importantly, how these promises could be implemented in practice. What is certain is that it is not going to be a smooth process, given the many political considerations in the BRI and the soft budget constraints and the guaranteed government bail-out for Chinese SOEs and state-owned banks. These factors could create insurmountable difficulties for the efforts to improve the financial sustainability of China's BRI investments and the debt sustainability in the receiving countries.

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