Contextualizing China's Belt and Road Initiative

Written testimony for the USCC submitted on January 19, 2018[1]

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[NOTE: *This testimony places the Belt and Road Initiative (BRI) in the larger strategic context of China's longstanding political-economic relations with the developing world. In keeping with the questions provided by commission staff, this testimony has four primary objectives: (1) explain China's strategic goals in the developing world and BRI's role in achieving them; (2) unpack and summarize the primary Beijing political-economic initiatives with an emphasis on BRI and China's political and soft power outreach; (2) explain how other countries have perceived and responded to China's development-first approach spearheaded by BRI; and (4) articulate some of the implications for the United States.*]

I. <u>Overview</u>

On May 14, 2017, over 1,500 people, including twenty-nine national leaders and delegates from 130 countries, gathered at the China National Convention Center in the Olympic Center in Beijing to hear President Xi Jinping's remarks opening the Belt and Road Initiative (BRI) Conference. "What we hope to create is a big family of harmonious co-existence," Xi said, then announced another 100 billion yuan ($14.49 billion) for the Silk Road Fund, bring the total to nearly $55 billion. Moreover, he added: "The China Development Bank and the Export-Import Bank of China will set up special lending plans respectively worth 250 billion yuan and 130 billion yuan to support Belt and Road cooperation." During the group photo, Xi was flanked by Russian President Vladimir Putin and Turkey's President Recep Tayyip Erdogan, who both spoke at the ceremony. Ethiopian Prime Minister Hailemariam Desalegn summed up the mood among the attendees: "China has taken the leadership in laying the foundations for the realization of our shared vision for an open, fair and prosperous world. Achievement of this vision will require our political commitment and a huge sum of resources."[1]

For centuries, Western observers have predicted that China would someday emerge as a major political and economic force in regional and world affairs and—as the 2017 BRI Conference and dozens of similar events demonstrate—that day has arrived.

The pace and scope of China's emergence has been breathtaking. Between 2000 and 2016, China's real GDP increased more than fourfold to roughly $11.4 trillion at the 2016 exchange

[1] This testimony is derived from the forthcoming book: Joshua Eisenman and Eric Heginbotham, eds., *China Steps Out: Beijing's Major Power Engagement with the Developing World* (London: Routledge, 2018).

rate;[2] its foreign trade climbed from $642 billion to $3.7 trillion (in 2016 dollars);[3] and its share of the global economy grew from 3.6 percent to 14.9 percent.[4] Over the last three years, Chinese FDI, which was about $70 billion in 2013, exceed $170 billion in 2016.[5] When Beijing abandoned isolation and began its economic "opening" to the world in the mid-late 1970s, even the most optimistic Chinese policymaker could not have predicted such a precipitous expansion of global engagement.

Under the "going out" strategy, which was first advanced in 1997 and formally initiated in 1999, Chinese firms have been transformed from novice newcomers to global powerhouses, and become deeply enmeshed in international trade, banking, and mergers and acquisitions.[6] The growth in China's trade with the developing world has consistently outstripped that with the developed world, and Beijing's policy banks (most notably the China Ex-Im Bank and China Development Bank) have deployed hundreds of billions in capital in an unprecedented global infrastructure financing campaign that dwarfs that of the World Bank.

After the 2009 global financial crisis, Chinese leaders came to believe that the historic trend towards multipolarity had accelerated and that developing states were becoming ever more important economic, political and military partners. China's new self-confidence was reflected in Xi Jinping's notion of "major power diplomacy with Chinese characteristics" and his call to shape the international environment more proactively.[7] China has become an increasingly active participant in international institutions, taking a leading role in United Nations peacekeeping operations and almost doubling its contributions to and vote share in the International Monetary Fund.[8] Beijing has also created and funded numerous Sino-centric regional organizations (e.g., the China-Africa Cooperation Forum and the China-Community of Latin American and Caribbean States Forum) that provide regional venues for Chinese leadership. Other organizations like the Asian Infrastructure Investment Bank (AIIB) enhance the perception that China has emerged as the champion of globalization, though it is unclear whether such institutions complement or challenge existing international institutions.[9]

Since 2013, Beijing's "going out" policy has been expanded into the ambitious BRI initiative championed by President Xi Jinping. To cope with excess industrial and construction capacity and gain higher returns, the financing of infrastructure has been accelerated under the BRI. To help Chinese state-owned and private firms take advantage of new economic opportunities in lesser-developed regions, China has policy banks and other funding mechanisms (e.g., the China Ex-Im Bank, China Development Bank, the China-Africa Development Fund, and the Silk Road Fund) to lend money to foreign governments to execute infrastructure projects employing Chinese firms. The Beijing-based Asian Infrastructure Investment Bank, unlike the others, is a multilateral institution, but it is also part of China's larger international development and trade promotion strategy. According to an official media outlet: "With the 'Belt and Road' initiative and other strategies serving as a powerful engine… China's overseas investment will continue to maintain a double-digit growth rate."[10]

Yet, China's ambitious push into the developing world, now headlined by BRI, has not been without setbacks and problems. China's economic slowdown, especially the sharp downturn after 2015, precipitated a drop in global commodity prices and raised new questions about the profitability of many government-driven commodity investments. Similarly, after making tens of billions in politically-driven loans at favorable rates to countries such as Venezuela, Zimbabwe, and Sri Lanka, China now faces problems recouping its money. The question is whether BRI will reverse these trends or, more likely, exacerbate them.

Asymmetric trade and investment relations have engendered concern among leaders in numerous developing countries, and, in some cases, drawn protests from local populations. China's growing hard power, combined with its more assertive approach to territorial and boundary issues in the South China Sea, has also caused some states around China's periphery to seek closer military or strategic ties with the United States and Japan. Farther afield, in the Middle East and to a lesser extent Africa, Beijing's commitment to neutrality and non-interference in regional disputes are increasingly being tested as its economic interests expand in ways that require it to behave like a more traditional major world power.

II. China's Strategic Objectives in the Developing World

There are various formulations of China's "core national interests" (核心利益), but all assume three overlapping objectives.[11] First, China's leaders seek to ensure the continued rule of the Communist Party; second, they seek to maintain and defend China's sovereignty and territorial integrity; and third, they want to maintain an international environment conducive to China's continued economic growth.

Despite propaganda efforts to portray Chinese policies as rooted in solidarity with the developing world, the drivers of Chinese policies remain primarily domestic, and regime survival remains Beijing's foremost objective, informing all other interests. The priority on regime survival is evident in the content and character of its diplomacy, party-to-party relations, defense of sovereignty norms in international politics, and in its near single-minded emphasis on economic development.[12] As Deng Xiaoping said in 1992: "Development is the hard truth" (发展是硬道理).[13] At Davos in 2017, Xi—in a comment reminiscent of both Deng and U.S. President Abraham Lincoln's Gettysburg Address—said: "Development is of the people, by the people and for the people."[14]

The emphasis on economic growth and domestic stability naturally shapes China's engagement with the developing world. Chinese leaders view economic growth and welfare as central to regime survival, and they view trade as a critical engine of growth. For more than a decade, developing countries have supplied the minerals, metals, timber and energy demanded by the Chinese industrial, construction and manufacturing sectors. To secure steady access to those resources, Chinese companies have, since the early 2000s, moved to purchase upstream energy and mineral assets, primarily in developing countries. These countries have also become important outlets for Chinese consumer products, enabling Chinese firms to build brand loyalties in emerging markets.[15]

Improved living standards are integral to Xi's "China Dream," with its goal of achieving a "moderately well off" society (小康社会) by 2021. For many years, officials in Beijing viewed rapid economic growth as essential to absorbing China's growing workforce and avoiding social instability. Since the Third Plenum of the Communist Party's 18th Congress, however, leaders have emphasized balanced growth, environmental protection, and eliminating structural imbalances within the economy. That said, old habits die hard. Local and many central government officials continue to use GDP growth rates as the yardstick of success. Moreover, Xi's "Made in China 2025," is a plan to comprehensively upgrade and strengthen the country's manufacturing capability. Nevertheless, as wage structures continue to shift in China and as environmental concerns mount, labor-intensive industries (e.g., textiles and leather goods) will continue to shift production to developing states.

The developing world is also a locus of Beijing's efforts to maintain or defend its "territorial integrity." After a "diplomatic truce" from 2008 to 2016, the competition for diplomatic recognition between Taipei and Beijing appears to have resumed with the election of Tsai Ing-wen in Taiwan. In its quest to contain separatist impulses in Tibet, China periodically sanctions countries and foreign organizations that give the Dalai Lama a platform or afford him anything approaching recognition.[16] Chinese activities to secure its claims to features in the South China Sea have included the use of hard power and coercive measures directly against rival claimants. China has also solicited public support from at least 66 mostly-developing countries for recognition of its maritime territorial claims in the South China Sea, and employed a variety of economic and political means to purchase the loyalty of the smallest and weakest states in ASEAN (Laos and Cambodia) to divide the organization and prevent unified opposition from coalescing.[17]

More broadly, China has found common interests with developing states on a range of political-economic issues (e.g., environmental priorities and trade-offs, trade policy, technology standards, and the form and function of international institutions) and has sought to partner with the largest of them to foster a more "democratic" international order. Interests on these issues often align across regime types. Despite India's long history of vibrant democratic governance, New Delhi's votes in the UN General Assembly on various issues are more closely aligned with those of Beijing than they are with Washington's.[18] In Beijing's case, support for norms related to state sovereignty and non-intervention are motivated by a desire to insulate itself from international condemnation, sanctions and intervention related to its human rights abuses and harsh policies toward minorities in Tibet and Xinjiang.

III. Structure of China's Political-Economic Engagement with Developing Countries

China's relations with developing countries display three principal characteristics: first, Beijing benefits from and sometimes exploits asymmetry in its relations with developing countries; second, China pursues a "package" approach – bringing economic, political, and other means to bear in a coordinated, albeit imperfect, manner; and third, Beijing advances its interests through a network of interlocking and self-reinforcing bilateral, regional, and global engagements. Each developing country's ability to derive benefits from its relationship with China depends primarily on its ability to develop and implement a coordinated national strategy that carefully considers the combined implications of these three characteristics over the short, medium, and long term. If a developing country ignores these realities or fails to consider their full implications, it is unlikely to achieve its own objectives vis-à-vis China; a much larger, richer, and generally, better coordinated state.

Asymmetric Engagement

Asymmetry is the most pervasive and enduring aspect of nearly all of China's bilateral relationships, a fact that then-Foreign Minister Yang Jiechi reminded a security forum of the Association of South East Asian Nations (ASEAN) of in 2010 when he said: "China is a big country and other countries are small countries, and that's just a fact."[19] Indeed, China's nominal GDP ($11.4 trillion in 2016) dwarfs every developing country and is more than double the combined GDP of India ($2.3 trillion), Brazil ($1.8 trillion), South Africa ($280 billion).[20] In 2016, Chinese exports made up more than half of all exports from the developing world.[21]

Although asymmetry is ever-present in China's relationships with nearly all developing countries, Beijing can choose to either highlight and exploit it or downplay it. China's comprehensive "package" approach (discussed immediately below) magnifies the perception of asymmetry, while egalitarian diplomacy and calls for "brotherhood" and "equality" diminish it. Regional forums like FOCAC and the China–Community of Latin American and Caribbean States (CELAC) Relations Forum invariably alternate locations between China and different partner countries in these regions. Symbolically, this places China on par with entire regions and practically it enhances Beijing's already disproportionate agenda setting power. Beijing never fails to play the impressive and gracious host, with banquets replete with constant references to solidarity, state-sovereignty, and the equality of all nation states.

Comprehensive Engagement

Chinese foreign policy involves "multi-centric, multi-layered and multi-pivotal sub-networks of regional and international cooperation that are interconnected and interwoven," explained former Vice Minister of Foreign Affairs He Yafei.[22] Chinese foreign policy also now emphasizes a broad array of collaborative enterprises including foreign aid, educational and cultural exchanges, media cooperation, military assistance and training, and political cadre training. Beijing looks to combine these elements (discussed individually below) into a comprehensive package that creates synergies among China's various interests and allows the state to target resources and apply leverage to achieve its objectives. The breadth of Beijing's "comprehensive diplomacy" is well illustrated in its November 2016 white paper on Latin America and the Caribbean, which lists five broad areas of cooperation (i.e., political, economic, social, cultural, and peace and security) subdivided into 37 specific programs.

China's economic diplomacy, party-to-party relations, military diplomacy, and cultural outreach is often woven into a package that appears irresistible. China's policy banks have become the developing world's go-to lenders. Between these, and its massive state-owned commercial banks, China has 20 of the largest 100 banks in the world (ranked by total assets).[23] China's state-owned and semi-private infrastructure and telecoms firms have become the face of the country's overseas presence, building railroads, dams, airports, highways, and fiber optic networks for dozens of countries.

To be sure, not all of China's overseas engagement is state directed—or even directly state supported. Chinese small and mid-sized Chinese entrepreneurs (which account for a rapidly growing, and often unaccounted for, share of overseas trade and investment) generally operate independently in the developing world.[24] Even large SOEs target deals based primarily on prospective profitability, and they have proven willing in rare cases to resist political pressure to invest in deals they deem unpromising.[25] Nevertheless, Beijing can influence investment decisions and frequently does so to further its political objectives.

While economic tools are perhaps the most persuasive in Beijing's toolkit, China's comprehensive engagement goes beyond economics, and aims to build a stable, multifaceted, and mutually beneficial set of bilateral relationships. Chinese leaders have recognized that broader relationship must be "high-quality" and go beyond profits to include a "sense of justice" (义利观).[26]

Interlocking Engagement

While all major states conduct diplomatic activities at the *bilateral*, *regional,* and *global* levels, China's engagement consists of a particularly tight latticework of institutionalized relationships, and its focus on creating or interfacing with regional organizations is distinctive in the degree, if not type, of effort involved. By building a dense network of interlocking relationships, Beijing hopes to build a stable and mutually reinforcing structure that will further its interests.

Although China's creation of regional organizations is among the most distinctive features of Beijing's approach to the developing world, its bilateral relations remain the foundation. Multilateral forums boost legitimacy and visibility, but binding deals are primarily pursued bilaterally. China's approach towards individual countries is tailored in accordance with Beijing's specific interests there. China's relations with nearby states are generally deeper and more complex, with a mix of political, and economic interests, and sometimes territorial disputes, at play. Beijing's more distant relationships, by contrast, tend to prioritize economic objectives. China's relations with emerging major developing powers (including the BRICS countries and the developing members of the G-20) cut across regional lines and also tend to be multidimensional—with several overlapping political, economic, and security components.

Across the developing world, Beijing has deepened its bilateral relationships and maintains "strategic partnerships" with some 67 states.[27] Within each region, Beijing places considerable emphasis on its relations with large and important anchor or "hub" states where circumstances of geography, politics or economics make relations with China particularly propitious. These relationships tend to receive more attention in Beijing and be relatively stable over time. In East Asia, they include Indonesia and Thailand; in South Asia, Pakistan and India; in Central Asia, Kazakhstan; in Africa, South Africa, Egypt and Ethiopia; in the Middle East, Iran; and in Latin America, Brazil and Argentina. This list is not definitive, and has and will continue to evolve over time. For example, some states, like Venezuela under Hugo Chavez, received special attention and financing from Beijing for a limited period of time for political reasons. Small, but strategically located states, like Cambodia and Laos, are more susceptible to Chinese influence, and have served as useful "nail-house" votes in consensus-governed ASEAN.

The pattern of deepening engagement with regional institutions is replicated across every developing region. Beijing established relations with ASEAN in 1991, and today is involved in eleven ASEAN ministerial-level mechanisms across a wide range of economic, political, cultural, and security areas. It has maintained an ambassador to ASEAN since 2008, and has participated in the China-ASEAN Free Trade Area since 2010.[28] In Latin America, China was admitted as a permanent observer to both the Organization of American States (OAS) and Latin American Parliament in 2004. In January 2015, Beijing and Latin American leaders held the inaugural meeting of the China-CELAC Forum, at which Xi Jinping established a target for Chinese investment in Latin America of $250 billion within ten years.[29] Notably, the CELAC forum, unlike the OAS, does not include the United States.

China's regional diplomacy in Africa is orchestrated largely under the Forum on China-Africa Cooperation (FOCAC), which convened its first Ministerial Conference in Beijing in October 2000. In 2006, FOCAC was elevated to a Ministerial-level Summit, with meetings held every three years. China and Arab partners established the China-Arab States Cooperation Forum (CASCF) in 2004.[30] The CASCF and China-Gulf Cooperation Council strategic dialogue established in 2010 have allowed Beijing to expand relations with the Sunni-dominated Gulf States, which had been limited by China's close relations with Shia Iran.[31]

Since the 1980s, China has become an increasingly active contributor to international institutions. China's participation reassures other states that it is committed to the international system, provides venues to advance Chinese interests, and helps "lock in" Chinese policymakers in ways that help reduce conservative domestic opposition to reform. China's expanded involvement in global institutions also serves to highlight and promote Beijing's efforts to lead the developing world by reforming and shaping global institutions. Beijing has pushed for years to change quotas and vote shares in the World Bank, IMF, and Asian Development Bank, although the process has been painfully slow.[32] In the World Bank, it has advocated greater transparency in the selection of the president and an end to Western dominance, and has consistently sought to expand the prominence of the G-20 vis-à-vis the G-7.[33]

IV. BRI and China's Development-first Political-Economic Engagement

BRI (i.e. concessionary debt financing)

Development with Chinese characteristics has gone global. BRI seeks to create a new Sino-centric era of globalization using both traditional tools of Chinese statecraft as well as new types of economic incentives and debt financing arrangements. For two decades, China has promoted a "going-out" policy among its SOEs. Financing for Chinese-built projects in developing countries comes from a variety of sources, the most important being China's policy banks established in 1994 to finance projects important to Chinese economic growth. The Export-Import Bank of China (China Ex-Im Bank) and the China Development Bank provide large volumes of soft loans to developing countries under the condition that they hire Chinese SOEs to complete projects.[34] The loan portfolio of these two banks and 13 regional funds exceed the $700 billion outstanding loans from all six western-backed multilateral banks combined (including the World Bank, Asian Development Bank, Inter-American Development Bank, European Investment Bank, European Bank for Reconstruction and Development, and African Development Bank).[35]

When Chinese leaders conduct summit meetings, they often travel with large business delegations and sign MoUs worth hundreds of millions if not billions of dollars. In Islamabad in April 2015, for example, Xi Jinping and Pakistan's President Nawaz Shari signed 51 MoUs worth nearly $28 billion as the first phase of a larger Pakistan-China Economic Corridor Project said to be worth more than $50 billion.[36] During the December 2015 FOCAC meeting, Xi Jinping pledged some $60 billion in funding support, mostly in the form of loans and export credits and $5 billion in assistance to Africa.[37] Once terms are reached with a host country, funds may be transferred directly into the Beijing-based bank accounts of China's state-owned enterprises, which execute the project using Chinese materials and labor.

The dollar values discussed at these meetings hold out the promise of profits and economic growth for smaller partner nations. But MOUs are, of course, not legally binding contracts and many do not reach fruition or remain decades in the future. Others involve deals for which negotiations had been ongoing (in some cases for years), but which are pushed forward to correspond with a political meeting or leaders' summit.

In October 2013, the BRI became the overarching framework for this effort. Somewhat confusingly, the "belt" portion is continental, while the "road" portion is maritime. The Silk Road Economic Belt (SREB) runs through Central Asia, West Asia, the Middle East, and Europe. The Maritime Silk Road (MSR) connects China to countries in Southeast Asia, Oceania, and parts of North and East Africa—the South China Sea, South Pacific, and Indian Ocean regions. Designed to improve connectivity between China and more than 60 countries, BRI is overseen by the National Development and Reform Commission, Ministry of Foreign Affairs, and Ministry of Commerce, all under the auspices of the State Council.[38] Projects include virtually all types of transportation infrastructure, including rail, roads, ports, airports, electricity generation, telecommunications and various other forms of connectivity.[39]

In October 2013, the same month that BRI was introduced, Xi Jinping announced China's intention to establish the AIIB, which will complement the BRI initiative. The AIIB began operations in December 2015 with 57 founding member states—37 from Asia and 20 outside of it.[40] Initial capital was $100 billion, about two-thirds of the capital of the Asian Development Bank and about half that of the World Bank.[41] Although the AIIB is headquartered in Beijing, its president reports to an international board, and although China holds the largest voting bloc (26 percent) it remains a minority stakeholder. Beijing has also created the Silk Road Fund, backed by China's sovereign wealth fund but open to private investors.[42] Established in December 2014, the Silk Road Fund is capitalized at roughly $55 billion.[43] The AIIB's slow start and the Silk Road Fund's limited scale means that the preponderance of financing for BRI projects come from China's policy banks.[44]

While there are many unanswered questions about the initiative, it is clear that BRI takes China's finance and infrastructure construction efforts to a new, and far riskier, level. Beijing intends to allocate at least $1 trillion to the initiative, and scores of multinational corporations, both Chinese and foreign, are angling take full advantage.[45] The framework has subsumed many projects that were being considered long before BRI was launched, but the unquestioned political backing implied by writing BRI into the CPC constitution may lead to more projects being launched with less careful assessment of likely risks and returns. Because these projects involve loans, heavy BRI funding may exacerbate the debt problems of already poor states and further burden deeply indebted Chinese banks. China now owns more than half of some African nations' foreign debt, and many expect Beijing will have to write off significant portions in the years ahead.

Investment

Developing countries play a central role in China's "going out" foreign investment strategy. As early as 1999, China had amassed about $155 billion in foreign reserves and was looking to gain returns while generating work for its SOEs.[46] That year, at the Fourth Plenum of the 15th National Party Congress, Jiang Zemin launched the so-called "going out strategy" encouraging firms to "establish branches overseas" and "explore international markets."[47] Subsequent decisions during the 2000s provided funding mechanisms to facilitate outward investment. China's move outward began slowly—and primarily involved SOEs in the extractive and construction industries—but has diversified and gathered momentum since 2010. China's non-financial FDI flow increased from $3.6 billion (in 2016 USD) in 2003 to some $141.2 billion in 2015—a real compound annual growth rate CAGR of 36 percent.[48]

According to official figures, as of 2015 about 57 percent of China's total (outward) FDI stocks were in developing states (excluding investment in offshore financial centers), with the largest accumulations in Asia (25 percent of total), Africa (12 percent), and Latin America (5 percent).[49] In some sectors, Chinese firms also have their own sizable war chests and may sometimes prefer to invest their own funds. Much of CNOOC's $15 billion 2012 purchase of Canada's Nexen, for example, came from CNOOC's own cash reserves.[50] Notably, although Chinese investment in all these regions has increased markedly over the last decade, it is often not the largest investor. For example, Chinese investments in Africa during 2014 accounted for seven percent of all FDI in the region, far less than France's 21 percent.[51] In 2015, Chinese investment in Africa dropped to just three percent of the global total.[52] China accounted for about 9.5 percent of total FDI in Southeast Asia in 2016, Japan accounted for about 14.5 percent and the United States for about 12 percent.[53] In short, China has gone from having virtually no FDI stake in these regions to being a major player. But it is not the singularly dominant actor it is sometimes portrayed as, but rather one among several important investors.

Trade

Another important BRI objective is expanding and promoting trade, which enables China to leverage comparative advantages to grow its economy—with attendant benefits for the Chinese people and state capacity. Trade growth is not necessarily purely, or even necessarily primarily, a function of state-led promotion activities, but Beijing is using BRI to tip the balance in favor of its firms and suppliers. Chinese corporations, including SOEs, private and semi-private firms, often work closely with state policy banks and diplomats, who are empowered to help promote exports. According to one analysis, Chinese commercial service attaches working in China's African embassies outnumber U.S. Foreign Commercial Service officers working in the region by some fifteen to one.[54]

The rapid expansion of Chinese trade has become a key driver of GDP growth. GDP grew by a real compound annual growth rate of 9.1 percent between 1978 and 2015, while trade increased by an average of 12 percent. Trade growth has slowed considerably since 2012, partly due to government policies designed to enhance domestic consumption and, more importantly, the slowing of the Chinese economy.[55] China's trade grew by a 3.52 percent in 2014, *shrank* by 9.85 percent in 2015 and shrank again by 4.02 percent in 2016.[56] These trends are even more pronounced in China's trade with developing countries. Private firms accounted for 38.1 percent of trade in 2016.[57]

For China, developing countries have become increasingly important raw material suppliers and are growing markets for its manufactured products. China's trade with developing countries has come to account for an increasing percentage of the country's overall trade volume. In 1990, developing countries represented only 15 percent of total Chinese trade, but by 2000, that figure had grown to 19 percent, and by 2010, it had reached 31 percent. After peaking around 34 percent in 2012, the percentage has plateaued, as China's economic slowdown has reduced the need for raw materials and the price of oil and metals like copper and iron ore has fallen. If and when commodity prices fully recover, developing countries are likely to once again regain their leading position.

The value of China's trade with the developing world was $29.4 billion in 1990 (measured in constant 2016 USD) and rose to $1.2 trillion in 2016 (about 33 percent of China's total foreign trade)—a real CAGR of 15.4 percent—compared to a 12.1 percent CAGR for China's total trade over that period. China's trade volume by region were: Southeast Asia, 12.4 percent of total Chinese trade; the Middle East, 5.5 percent; Latin America, 5.7 percent; Africa, 4.1 percent; South Asia, 3 percent; and Central Asia, 0.9 percent.[58]

Economic Assistance

China provided substantial economic assistance to developing states during the 1950s, 1960s, and early 1970s, but cut back on those expenditures in the late 1970s, 1980s and 1990s as it sought to rebuild its own economic position. Over the last decade, however, foreign aid has reemerged as an important part of the Chinese foreign policy toolkit, and Beijing released white papers on the subject in 2011 and 2014. The budget for foreign assistance has grown rapidly over the last decade, with an average annual increase of 29.4 percent between 2004 and 2009. Between 2009 and 2012, China's aid disbursements totaled $14.4 billion, or about a third of China's total aid from 1950 to 2008.[59] Unfortunately, the Ministry of Commerce, which coordinates China's assistance programs, does not provide year-on-year tracking, complicating systematic evaluation.

Chinese economic assistance comes in three varieties: grant aid (36 percent of the 2009-2012 total); interest-free loans (8 percent); and concessional loans (56 percent).[60] These funds go to support a wide range of programs: emergency assistance, technical aid and instruction, health care and medical facilities, low cost housing, education, state capacity building, infrastructure development, and environmental protection. In terms of distribution, some 52 percent went to Africa over this period, 31 percent to Asian states, and 8 percent to Latin America and the Caribbean.[61]

China's approach to foreign assistance differs in several respects from the members of the OECD's Development Assistance Committee (DAC), private Western donors like the Gates Foundation, and multilateral institutions like the World Bank. Rather than poverty alleviation, China's assistance, particularly its concessionary loan aid, is primarily focused on infrastructure development tied to Chinese business contracts. It is nearly always distributed on a state-to-state basis. Unlike Western countries and institutions which often place economic or political conditionality on their aid, Chinese aid does not require subsequent audits and comes with "no political strings attached."

The predictable result is that Chinese aid is often easier for corrupt foreign leaders to "capture" and channel towards politically important regions, constituencies, and cronies.[62] While China's foreign aid programs could focus more on grants and interest free loans and made more transparent to safeguard against abuse by recipient governments, the approach taken by the DAC states and the Bretton Woods Institutions has also faced criticism. Angus Deaton, who won the 2015 Nobel Prize in Economics for work on poverty, argues that the West's approach to aid "undermines what poor people need most: an effective government that works with them for today and tomorrow."[63] Some therefore favor of China's "development first" approach, with its focus on state capacity and infrastructure.[64]

V. <u>Soft Power with and Political Outreach</u>

Beijing's impetus to become a "cultural major power" (文化大国) predates Xi. A broad conceptual framework was adopted in 2004 under the official formulation "China's peaceful rise," and a subsequent white paper was issued in 2011, as both a guide for Chinese policymakers and an effort to reassure anxious foreigners. Since 2013, however, Xi Jinping has spoken repeatedly on the need to increase China's "soft power" (软实力) by, among other things, creating a compelling Chinese narrative and strengthening Beijing's capacity to convey its message overseas.[65] "Soft power" is the ability of one nation to shape the preferences of others through its appeal and attraction at the popular, elite, or government levels.[66] Because soft power helps shape others' preferences, it increases the perception of congruence between Chinese interests and those of others.[67]

According to Chinese analysts, the nation's history makes it a "cultural major power" with great natural advantages.[68] In 2004, Beijing launched the Confucius Institute program to cultivate the study of Chinese language and culture abroad. According to the Confucius Institute Headquarters website, in 2016 there were 500 institutes around the world. Although these are clustered in developed countries, with 109 in the United States alone, many developing states also host institutes. Skeptics question whether Beijing-backed Confucius Institutes are being used to influence university research agendas and impinge on academic freedoms.[69]

China promotes other types of "person-to-person" exchanges, including foreign students studying in China. Beijing sponsors tens of thousands of foreign youths for training both in their home countries and at Chinese universities and vocational schools. According to the Ministry of Education, there were 442,773 international students studying in China in 2016, up from about 290,000 in 2011. Of foreign students in 2016, some 49,022 received scholarships from the

Chinese government, an increase of 20 percent from 2015.[70] In 2016, more than 264,976 foreign students in China hailed from Asia, but thousands of students are from other developing regions. For at least two consecutive years, the greatest increase was in the number of students from Africa, who numbered some 61,594 in 2016, up 23.7 percent from 2015. China is looking to expand job opportunities for graduates, so it can retain and utilize these young Chinese-speaking foreigners.[71]

China's influence in developing countries has expanded under President Xi, who in 2014 exhorted his comrades: "We should increase China's soft power, give a good Chinese narrative and better communicate China's messages to the world."[72] Chinese language schools, media training, cultural exchanges, educational and training programs, and other forms of aid and assistance have increased China's soft power in many countries.[73]

Meanwhile, Beijing is spending more time and resources hosting and visiting counterparts from developing countries' political parties than ever before. Outreach by the International Department of the Central Committee of the Communist Party of China (ID-CPC) is a historical and ongoing feature of Chinese foreign policy and supplements the diplomacy conducted by state organs (e.g., the MFA) and leaders. The Party's political outreach generally looks to engage in ways that avoids the appearance of intervention in domestic affairs. In autocracies, the ID-CPC may avoid interaction with the opposition, while in liberal democracies, it maintains ties with both ruling and opposition parties.

In Africa, the CPC has expanded its host diplomacy, cadre training, and outreach to political parties in Africa and throughout the developing world. China's training programs are generally oriented towards state capacity building and include, for example, training programs on the management of agricultural technology programs. Other elements, like the political cadre training done by the International Department of the CPC Central Committee and media training programs run by the official Xinhua News Agency, are explicitly political and are intended to improve foreign perceptions of China and legitimize the ruling party. In 2014 and 2015, some 2000 officials of South Africa's African National Congress (ANC) were trained by the CPC, and Beijing is financing the ANC Political School and Policy Institute, modeled on the China Executive Leadership Academy in Shanghai.[74] Ethiopia was perhaps the earliest and most eager student of Chinese cadre training, and has dispatched delegations regularly to China since 1994.[75] During a public talk at Fudan University in Shanghai in May 2017, Arkebe Oqubay, a Minister and Special Advisor to the Prime Minister of Ethiopia, identified party-to-party relations as the first of three Sino-Ethiopian links (along with government-to-government and people-to-people).[76]

Over the last decade, led by Xinhua and CCTV, China's state-run media has advanced an initiative to enhance China's influence and international image.[77] Since 2005, Xinhua has emphasized cooperation, content sharing, and media training programs with dozens of news outlets throughout the developing world.[78] China wants to improve younger generations' perceptions of its political system and gain elite support to counter what Beijing sees as Western efforts to portray Chinese practices in an unfavorable light. In 2017, for instance, Renmin University in Beijing hosted a 10-month development studies and media exchange with 48 students from Africa, South Asia, and Southeast Asia. Training topics include China's political, cultural, media and economic studies. Counselor Liu Yutong, Chief of the Public Diplomacy Division at the MFA's Information Department, welcomed the journalists with a speech about Chinese stability and growth—and questioned the wisdom of Britain's exit from the EU and the U.S. election of Donald Trump.[79]

VI. Evaluating BRI and Countries' Perceptions

Chinese engagement with the developing world has undoubtedly helped Beijing enhance the perceived legitimacy of the CPC, improve living standards for the Chinese people, and expand Beijing's power and influence around the world. China has been largely successful in achieving these aims, but it has also not been without setbacks, and the scale of risk has risen together with its overseas profile in recent years. China's BRI and the "going out" strategy before it open developing markets to Chinese-made products and expanded access to the raw materials China needs to meet domestic demand. Its investments and loan financing for infrastructure, catalyzed through BRI initiative, have provided sustained opportunities to redeploy China's considerable productive capacity in the construction, telecom and other sectors. All of this facilitates China's pursuit of its centenary goals, the lifting of living standards for the Chinese people, the power of the Chinese state, and (most importantly for China's leaders) the perceived legitimacy of the Communist Party.

While China's BRI has been a diplomatic success to date, its future is uncertain. At home, Chinese leaders understand that economic growth is overly dependent on investment and exports, though they remain ambivalent about rebalancing towards consumption-led growth. At the same time, Beijing's policy banks regularly finance projects regarded as too risky by Western counterparts and the decline in commodities prices has exacerbated that risk.[80] China's existing loans to friendly governments in Zimbabwe, Venezuela, and Sri Lanka already portend tens of billions of dollars in potential losses. China provided roughly $60 billion in loans and aid to Venezuela between 2007 and early 2016, and, as of mid-2016, the latter still owed China $20 billion. But with oil prices stuck near $50 per barrel and Venezuela unable to service its debts fully, Beijing finally cut off new lending in September 2016.[81]

BRI represents a massive and unprecedented expansion of connected lending to international borrowers that enmeshes the already deeply indebted Chinese banking system in some of the world's most precarious economic and political environments. The lending program's sheer size requires Chinese government and party organs, many with little experience in international operations, to vet scores of projects across a myriad of regulatory, linguistic, and cultural environments. Many poor countries, especially in Africa, are happy to take cheap Chinese loans now and let future leaders and citizens pay them back. China's response has often been to grant loan forgiveness and then provide more loans, creating a serious moral hazard problem. Many governments are banking on China's continued largesse and are thus happy to take whatever they are offered. However, Beijing, which saw its foreign reserves drop by more than 20 percent between 2014 and 2017, cannot write off bad loans *ad infinitum*.

BRI could also open new opportunities for fraud and corruption. China, which itself ranks an unimpressive 83 on Transparency International's 2015 corruption index, is building hundreds of projects in some of the least accountable countries in the world, such as Turkmenistan (154), Kyrgyzstan (123), Cambodia (150), and Myanmar (147). On an OECD 8 point scale of risk by recipient country, the portfolio of states that China's banks extended loans between 2013 and 2015 entailed an average risk rating a full point higher (i.e., more risky) than the World Bank's.[82] Xi himself seemed to recognize the challenges when he called for a "stable, sustainable and risk-controllable financial security system" to supervise the BRI initiative.[83]

In the political realm, Chinese diplomacy has generally been successful in developing relationships and gaining influence. Beijing has certainly seen failures and setbacks, and has addressed such problems by expanding the depth and breadth of its bilateral political relations with developing states and through existing and newly created multilateral regional organizations. By institutionalizing relations via diplomatic arrangements, party-to-party dialogues, economic agreements, military forums, and person-to-person exchanges, Beijing has created numerous overlapping buffers that enable the rapid return to normal relations if unexpected crises disrupt the relationship.

China's overseas image is generally favorable, though it varies widely, depending on location and issue. According to a 2015 Pew survey conducted in 27 countries, an average of 55 percent of respondents hold a favorable image of China, compared to 69 percent for the United States. China is viewed most favorably in Africa (average of 70 percent in nine countries) and Latin America (57 percent average in six countries), while the perception is less positive in regions closer to China, where security concerns weigh heavily, and in the Middle East, where many have reservations about China's treatment of its Muslim Uighur population. Those surveyed also had a dim view of China's respect for human rights, with just 34 percent having a favorable impression.[84]

Influence, which might be defined as the ability to bring about changes in another state's intended behavior in ways that advance one's own aims, is notoriously difficult to measure, as it involves counter-factual analysis. That said, China appears to have successfully influenced other states on issues of marginal importance to the other state, where the costs of taking the desired action are small. Vague official statements supporting China's position on the South China Sea, for example, are costless for African and Middle Eastern states. Similarly, acquiescence to Beijing's single-minded efforts to marginalize Taipei and the Dalai Lama, also have minimal political costs for states beyond China's immediate periphery. South Africa, however, paid some price for acceding to China's demands when it refused the Dalai Lama a visa, prompting the cancelation of a conference of Nobel laureates in Pretoria.[85]

There are few clear cases of China's ability to translate its combined economic, political, military and soft influence into favorable outcomes when the stakes are high for the other state. However, China's efforts to minimize opposition to its consolidation of its territorial claims in the South China Sea arguably represent a case of at least partial success. Beijing has achieved a *fait accompli* in the South China Sea by reclaiming 3,200 acres of land on seven features and thereby turning reefs and rocks into significant military outposts.[86] Such measures have alarmed the states most directly affected, including Vietnam and the Philippines, and fueled wariness in larger regional states like Indonesia and Malaysia. Beijing has responded by offering a blizzard of trade and aid proposals and by leveraging its asymmetric relationship with Cambodia and Laos to thwart joint statements by ASEAN.

China's impact on the economic, governance, and environmental welfare of the partner states in the developing world is mixed. China is, by far, the largest trade partner of developing states in every part of the world, and the loan portfolio of its policy banks and regional funds exceeds that of all Western multilateral banks combined.[87] Chinese activity is stimulating growth and building infrastructure in regions that are chronically short of capital and investment. Even in Southeast Asia, where Japan, the United States, and other Western countries are major actors, most states suffer from infrastructure financing deficits.[88] In sub-Saharan Africa, China's aid and investments are distributed across a wider range of recipient states than is assistance from Western states and international organizations. Some of the difference is explained by Beijing's willingness to engage the least savory African regimes, but it also reflects the more limited (and focused) interests of Western firms, states, and international organizations in Africa.

Needless to say, countries have been affected differently by their engagement with China. During the commodities boom of the 2000s and early 2010s, growth rates rose rapidly among resource-rich countries. At the same time, imports from China had significant displacement effects on domestic African and Latin American producers of labor intensive manufactured products, like textiles and food processing.[89] The pattern was more mixed in East Asia, where the region's integrated production chains contribute to the specialization among states.[90] Roughly 50 percent of Indonesian exports to China are raw materials, while Taiwan, Korea, and Malaysia export mostly intermediate, capital, or consumer goods.[91]

China's corporations have a poor record of environmental protection at home, and they have contributed to degradation overseas, especially when local governments suffer from poor capacity, weak oversight, or endemic corruption. Some firms have been accused of cutting corners, ignoring safety standards, using secondhand or low-quality materials and equipment, and building environmentally destructive projects. Complaints have come from Laos, Vietnam, and Cambodia regarding environmental damage and droughts from Chinese hydropower projects along the Mekong River; from Indonesia regarding an ill-fated, over-budget coal power plant and a failed high-speed rail project; from Myanmar regarding Chinese firms clear-cutting forests; and from Korea and West Africa about harm done to the marine environment by Chinese trawlers fishing practices.[92]

Facing growing public resentment at home, the Chinese government has become more attuned to environmental issues. It has passed new environmental regulations and promoted the State Environmental Protection Administration to ministerial status, changing its name to the Ministry of Environmental Protection in 2008.[93] Both the Chinese state and its companies have adopted or signed international compacts designed to protect the environment overseas.[94] Nevertheless, enforcement responsibilities and oversight remains weak at home, and Beijing has even more difficulties policing its corporations – especially small- and mid-sized private firms – overseas. China's lack of conditionality, lax oversight, and poor corporate citizenship contribute to, or at least do not discourage, rent seeking and corruption in partner states.[95] The problem is likely to worsen as rising labor costs in China push more "dirty" manufacturing to relocate to cheaper and less well-regulated developing countries.

China's expansion in the developing world may also adversely affect the spread of liberal values. After a remarkable wave of democratization from the mid-1970s to the mid-2000s, the tide appears to have turned. According to the 2017 Freedom House report, those countries experiencing a net decline in freedom have exceeded the number experiencing a net gain every year between 2006 and 2016. In 2016, 67 countries saw declines while just 36 improved.[96] In some countries, like Russia, Venezuela, and Zimbabwe, autocrats have maintained the facade of democracy (e.g., elections and private press outlets) while stripping them of all meaning.[97] Others, like Ethiopia, seem to have more borrowed directly from China's authoritarian state-led development model.

China's attractiveness as an economic model has increased due to its sustained economic growth and as neoliberal economic practices (broadly known as the Washington Consensus) have lost the confidence of policymakers in developing states – particularly in the wake of the global financial crisis of 2008. More recently, however, reduced growth rates and rising debt levels in China have diminished the attractiveness of the "China model." Moreover, with the decline in commodities prices, Chinese investments and debt financing for resource-related infrastructure has saddled some countries with unsustainable debt again diminishing the popularity of China as both partner and model. Only time will tell whether the billions of dollars Beijing has spent on enhancing and projecting its soft power – the Confucius Institutes, CPC cadre training programs, Xinhua media training, film festivals, think-tank exchanges, student scholarships, etc. – will succeed in improving perceptions of China.

Despite these efforts to enhance Chinese "soft power," however, many countries on China's periphery continue to harbor deep concerns about Beijing's long-term ambitions and others are deeply ambivalent about excessive dependence on trade with and investment from China. Addressing these concerns while pursuing Beijing's material goals will challenge Chinese foreign policy leaders for the foreseeable future.

VII. Implications for the United States

Beijing and Washington's relations with the developing world are not primarily zero-sum. To a significant extent, interests are parallel—that is, separate and non-overlapping in either a competitive or cooperative sense. American firms benefit from improved global growth and improved economic efficiencies that result from China's policy banks financing tens of billions of dollars' worth of transportation infrastructure around the developing world. Chinese raw material purchases from Africa, for instance, are a link in the global supply chain. They supply Chinese manufactures, which, in turn, sell their finished products to furniture stores from Boston to Beijing to Bangkok. But although Washington and Beijing pursue their economic and political interests vis-à-vis developing states in ways that often neither directly benefits nor harms the other, that dynamic could change if the Sino-U.S. relationship evolves dramatically for the worse or if the BRI precipitates a massive raft of loan defaults that destabilizes the international economic system.

In some important respects, American and Chinese interests coincide. Both benefit from stability and prosperity in the developing world, yet they attribute these outcomes to different sources. Washington has long maintained that free and fair elections and an open society are essential for long-term political stability, while Beijing believes that economic development is the primary cause.[98] The bloody aftermath of the Arab Spring has dampened Washington's interest in actively supporting democratic change through revolutionary means, though it continues to promote democratic and liberal values. After the election of Donald Trump, it remains to be seen whether Washington will revert to traditional modes of active interventionism or adopt a more isolationist "America first" foreign policy.

The United States would be well served to deepen its political and economic presence and influence in the developing world. By many standards, U.S. engagement with and assistance to the developing world in areas from health care and food aid, to institution-building, environmental leadership, military engagement, media, NGOs, and a raft of other areas remain deeper and better considered than China's. Yet many of these efforts gain little attention and are not well understood. Of much greater concern, U.S. efforts could be severely undercut should funding for the U.S. Department of State, the U.S. Agency for International Development, and other parts of the U.S. foreign policy establishment be significantly reduced. The U.S. government is already far less involved in promoting trade and investment than China. This puts U.S. firms at a disadvantage in competing with Chinese counterparts, and it undermines the larger effort to maintain U.S. relevance in the developing world. Washington should increase funding for the Foreign Commercial Service, U.S. Ex-Im Bank, and other federal programs that improve U.S. corporations' international competitiveness. The United States has the resources to maintain its global leadership position; the question in these uncertain political times is whether it will choose to do so.

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