

## China

# Our bulldozers, our rules

THE first revival of the Silk Road—a vast and ancient network of trade routes linking China's merchants with those of Central Asia, the Middle East, Africa and Europe—took place in the seventh century, after war had made it unusable for hundreds of years. Xi Jinping, China's president, looks back on that era as a golden age, a time of Pax Sinica, when Chinese luxuries were coveted across the globe and the Silk Road was a conduit for diplomacy and economic expansion.

The term itself was coined by a German geographer in the 19th century, but China has adopted it with relish. Mr Xi wants a revival of the Silk Road and the glory that went with it.

This time cranes and construction crews are replacing caravans and camels. In April a Chinese shipping company, Cosco, took a 67% stake in Greece's second largest port, Piraeus, from which Chinese firms are building a high speed rail network linking the city to Hungary and eventually Germany.

In July work is due to start on the third stage of a Chinese designed nuclear reactor in Pakistan, where China recently announced it would finance a big new highway and put \$2 billion into a coal mine in the Thar desert.

In the first five months of this year, more than half of China's contracts overseas were signed with nations along the Silk Road—a first in the country's modern history. Politicians have been almost as busy in the builders' wake. In June Mr Xi visited Serbia and Poland, scattering projects along the way, before heading to Uzbekistan. Last week Russia's president, Vladimir Putin, made a brief visit to Beijing; He, Mr Xi and Mongolia's leader promised to link their infrastructure plans with the new Silk Road. At the time, finance ministers from almost 60 countries were holding the first annual meeting in Beijing of an institution set up to finance some of these projects, the Asian Infrastructure Investment Bank (AIIB). Like a steam train pulling noisily out of a station, China's biggest foreign economic policy is slowly gathering speed.

Chinese officials call that policy "One Belt, One Road", though they often eviscerate its exotic appeal to foreigners by using the unlovely acronym OBOR. Confusingly, the road refers to ancient maritime routes between China and Europe, while the belt describes the Silk Road's better known trails overland (see map). OBOR puzzles many Western policymakers because it is amorphous—it has no official list of member countries, though the rough count is 60—and because most of the projects that sport the label would probably have been built anyway. But OBOR matters for three big reasons.

First, the projects are vast. Official figures say there are 900 deals under way, worth \$890 billion, such as a gas pipeline from the Bay of Bengal through Myanmar to southwest China and a rail link between Beijing and Duisburg, a transport hub in Germany. China says it will invest a cumulative \$4 trillion in OBOR countries, though it does not say by when. Its officials tetchily reject comparison with the Marshall Plan which, they say, was a means of rewarding America's friends and excluding its enemies after the Second World War. OBOR, they boast, is open to all. But, for what it is worth, the Marshall Plan amounted to \$130 billion in current dollars.

Next, OBOR matters because it is important to Mr Xi. In 2014 the foreign minister, Wang Yi, singled out OBOR as the most important feature of the president's foreign policy. Mr Xi's chief foreign adviser, Yang Jiechi, has tied OBOR to China's much touted aims of becoming a "moderately well off society" by 2020 and a "strong, prosperous" one by mid-century. Mr Xi seems to see the new Silk Road as a way of extending China's commercial tentacles and soft power. It also plays a role in his broader foreign policy thinking. The president has endorsed his predecessors' view that China faces a "period of strategic opportunity" up to 2020, meaning it can take advantage of a mostly benign security environment to achieve its aim of strengthening

its global power without causing conflict. OBOR, officials believe, is a good way of packaging such a strategy. It also fits with Mr Xi's "Chinese dream" of recreating a great past. It is not too much to say that he expects to be judged as a leader partly on how well he fulfils OBOR's goals.

Third, OBOR matters because it is a challenge to the United States and its traditional way of thinking about world trade. In that view, there are two main trading blocs, the transatlantic one and the transpacific one, with Europe in the first, Asia in the second and America the focal point of each. Two proposed regional trade deals, the Transpacific Partnership and the Transatlantic Trade and Investment Partnership, embody this approach. But OBOR treats Asia and Europe as a single space, and China, not the United States, is its focal point.

Mr Xi first spoke of a new Silk Road during a visit to Kazakhstan in 2013, a year after he took power. The first contracts bearing OBOR's name—about 300 of them, including a huge hydropower plant in Pakistan—followed in 2014, though many of those deals were already well advanced. The past two years have seen a frenzy of institution building. Mr Xi has set up a "small leading group" to oversee OBOR. This is an informal high level body linking government and party organisations. Its boss is Zhang Gaoli, who is a member of the Politburo Standing Committee, the party's innermost circle. It also includes the leadership's chief spin doctor and a deputy prime minister responsible for foreign trade. All the main bits of the bureaucracy have been corralled into OBOR.

A financial structure to support it has also taken shape. In 2015 the central bank transferred \$82 billion to three state owned "policy banks" for OBOR projects. China's sovereign wealth fund backed a new Silk Road Fund worth \$40 billion and the government set up the AIIB with \$100 billion of initial capital. The bank is not formally part of OBOR but the loans approved at its first general meeting—roads in Pakistan, Tajikistan and Uzbekistan, for example—are all in Silk Road countries. Now the rest of the Chinese state is mobilising. Two thirds of China's provinces have emphasised the importance of OBOR for their development. For example, Fuzhou, the capital of coastal Fujian province, has told its companies to "start businesses in the countries and regions along the maritime Silk Road"; It has set up a free trade zone to attract firms from such countries in South East Asia. Many big state owned enterprises (SOEs) have an OBOR department, if only in the hope of getting money for their projects. As a result, China's foreign direct investment (FDI) is increasingly going along the Silk Road. In 2015, by official reckoning, its FDI in OBOR countries rose twice as fast as the increase in total FDI. Last year 44% of China's new engineering projects were signed with OBOR countries. In the first five months of 2016, the share was 52%.

China's approach to investment seems to be changing, too. Its OBOR contracts are now more likely to involve Chinese firms managing the infrastructure they build, rather than (as in the past) building them and simply handing them over. In theory, this should give China an interest in working for the long term in Silk Road countries. Yet while OBOR gathers momentum it is also encountering problems. These are especially glaring in Southeast Asia. China is planning a 3,000km (1,900mile) high speed rail line from Kunming, in its southwest, to Singapore. But in June talks with Thailand over its section of the line broke down; The Thais said they would build only part of the project, and would finance it themselves. There have been many other such failures. Also worrying are signs that there are not yet enough viable projects for the vast sums being earmarked. The Silk Road Fund was set up to invest in infrastructure abroad. But two of its first investments were in initial public offerings by Chinese firms in Hong Kong.

Problems have arisen too with OBOR's leadership. Mr Zhang, the most senior person in charge, is thought to be out of favour after blotting his copybook in March by saying that the economy had had "a tremendous start" to 2016. This contradicted the views of people close to Mr Xi who argue that a slowdown is necessary. The travails of the European Union—and especially of Britain, which has claimed to be enjoying a "golden age" of relations with China—might make Chinese leaders nervous about Europe's willingness to support OBOR, though it might also in the long run make it easier for China to exploit rivalry between European countries when doing deals with them.

More broadly, China has many competing bureaucratic interests at stake in the Silk Road project.

Reconciling them will be tough. OBOR is supposed to extend Chinese commercial influence, reduce the Chinese economy's dependence on investment in infrastructure at home and export a little of China's vast excess capacity in steel and cement. Tensions between these aims are inevitable. Should China give priority to underperforming provinces or underperforming SOEs? Can it help poor western provinces while reducing its spending on domestic infrastructure? Ready or not, here they come.

All that said, there are reasons for thinking the new Silk Road will be paved, albeit not with gold. Most important, Asia needs new infrastructure—about \$770 billion a year of it until 2020, according to the Asian Development Bank. This demand should eventually ease today's worries about a lack of projects. Bert Hofman, the World Bank's chief in Beijing, adds that individual countries will benefit more if they align their plans with one other and with China. It does not pay to plan and build separately. Next, China needs OBOR. At home, its businesses are being squeezed by rising costs and growing demands that they pay more attention to protecting the environment. It makes sense for them to shift some manufacturing overseas—as long as the infrastructure is there. Lastly, Xi Jinping needs it. He has made OBOR such a central part of his foreign policy and has gone to such lengths to swing the bureaucracy behind the project that it is too late to step back now.

None of this means the new Silk Road will be efficient, nor does it mean China's plans will always be welcome in countries suspicious of its expanding reach. But the building blocks are in place. The first projects are up and running. OBOR is already beginning to challenge the notion of Europe and Asia existing side by side as different trading blocs.