

China's Belt and Road Initiative: Hopes and Bumps along the Road*

Gerard Roland
UC Berkeley, CEPR and NBER

Keywords: China, globalization, capitalism, communism, trade,
JEL codes: P00, P1, P2, P3, P5

Abstract:

Pranab Bardhan has been a keen observer of China's reforms. This paper analyzes China's Belt and Road Initiative (BRI), its goals for the Chinese Communist Party, its potential effects on the international economy as well as initial results of BRI. I argue that evaluation of BRI needs to be done in light of its stated objectives, not standard efficiency or developmental goals. Chinese leaders aim foremost at stronger integration in the world economy to prevent China's growth from falling behind that of the world economy. The BRI should deliver China better access to natural resources as well as helping it to promote export growth. Difficulties in the implementation of the BRI goals are a useful indicator of the governance problems facing the Chinese Communist Party in China itself.

1. Introduction.

Pranab Bardhan has been studying closely the evolution of China's economic system in an international comparative perspective. His 2010 book *Awakening Giants, Feet of Clay: Assessing the Economic Rise of China and India* raised a number of important issues related to the specificities of China's growth success.

Recently, many questions have been raised about the Belt and Road Initiative (BRI)¹, its strategic significance for Chinese leaders and its geopolitical implications. Are these just economic development initiatives that other countries are invited to join, as is often stated in the Chinese media? Are these instead first steps towards China attempting to wrestle world hegemony away from the US as its economic power becomes stronger? Five years after it started, reports have started to appear about the results of some of the investments made under the BRI. What do we know? How to evaluate those investments?

To answer these questions, one needs to understand the long term strategy of the Chinese Communist Party (CCP). This strategy is quite original. After Mao's death, under Deng Xiaoping's leadership, the CCP engaged in reforms transforming China from a socialist centrally planned economy to a modern thriving market economy. The goal of these reforms was to generate economic growth in order to keep the CCP in power. Given the success of the Asian tigers in the 60s and 70s (mostly Japan, South Korea, Hong, Kong Singapore), Deng thought that continental China could not afford to stay poor. Otherwise, people would revolt against the CCP, and the latter could lose power. Deng thus embarked on a historically completely new innovation: the introduction of a capitalist economy under a politically communist regime. The Chinese economy has had spectacular growth rates for 40 years since these reforms were introduced, and one can say that Deng's objective (the survival of the CCP) was well achieved. Nevertheless, Chinese leaders are very much afraid that this will not last. They know that growth eventually slowed down in successful East Asian economies. Japan has even had over two decades of quasi-stagnation. Even though the slowing down of Chinese growth is a certainty, Chinese leaders want to make sure that the growth of the Chinese economy does not fall behind that of the rest of the world. It is in that context that we must see the Belt and Road Initiative. This initiative aims at further integrating the Chinese economy in the world economy. This will be done by creating trade routes with the rest of the world that will secure imports of natural resources needed in China, given its relative scarcity of natural resources. These trade routes should also be used to export Chinese goods abroad and broaden China's export performance. Chinese leaders want to protect these trade routes from blockade by establishing a military (mostly naval) presence at various critical spots. This is an interpretation of BRI that is based on the nature of the Chinese regime and the fundamental strategic goals of its leaders. It could be mistaken for geographical expansionism, but we think that would be a mistaken

¹ Previously, it has been called the One Belt one Road" initiative (OBOR) or the "new

interpretation that could lead to aggressive moves that could fatally endanger world peace.

We develop our argument in several steps. In section 2, we explain the nature of the economic system in China: a capitalist regime under the leadership of the Communist Party. On that basis, we explain in section 3 the international strategy of Chinese communist leaders. In Section 4, we discuss how to evaluate the BRI in that light. Section 5 concludes.

2. The nature of the Chinese economic regime

In the light of stagnation of the USSR in the seventies and the chaotic (and lunatic) Maoist management of the economy since 1958, Deng Xiaoping thought that the best strategy to consolidate the power of the Chinese Communist Party (CCP) was to introduce the market economy in continental China, following the examples of Taiwan, Hong Kong and Singapore, all places where a large Chinese population or diaspora had enjoyed prosperity and economic growth. Deng was pragmatic. He had observed the economic success of Taiwan, Hong Kong and Singapore (called the Asian tigers at the time), and argued that if the Communist Party was not able to deliver growth rates as robust as those countries, it would inevitably lose power. This vision proved to be quite prophetic. In the late seventies, it was not yet clear that the Soviet system would collapse and that communist regimes in Central and Eastern Europe would disappear. Many of Deng's colleagues wished a return to the central planning system of the fifties. This seemed to be a safer bet, advocated by Party elders like Chen Yun, Deng's main opponent when it came to market reforms. The compromise they agreed on was to experiment with decollectivization in the countryside and to incentivize peasants via the "Household responsibility system": Maoist communes (large socialist cooperatives regrouping several villages) were disbanded and households received land with a 15 year lease. They were obliged to deliver a fixed quota of grain to the state at a fixed price, but were allowed to freely produce and sell at free prices on markets any additional output they produced. The implementation of the household responsibility system proved to be phenomenally successful and created momentum for further reform leading to China's growth miracle (on the political economy of reform momentum in China, see Dewatripont and Roland, 1995, Xie and Xie, 2017).

Deng eventually used the power of the CCP to unleash market forces in China relying mainly on two elements: government decentralization and yardstick competition (meritocracy).² Contrary to superficial reports, China's economic success was not due to the State withdrawing from the economy, but to the CCP using all possible instruments at its disposal to achieve high rates of economic growth. Not surprisingly, this process eventually reinforced the power of the CCP in all spheres (military, education, press,...) instead of decreasing it, which had been Deng's avowed goal all along. Private entrepreneurs can since 2001 become CCP members, a move that can be seen as a way for the CCP to keep control over the private sector.

² See the classical paper by Xu, 2011 for the consensus view among researchers on the reasons behind China's success.

The initial thinking on Chinese reforms was that political reform would sooner or later follow economic reform. After all, the Soviet Union did have a political transition shortly before economic transition. The sequencing of reforms seemed to be different in China, but most observers thought that economic reforms would lead to gradual political liberalization. In hindsight, that view was deeply mistaken. If anything, the opposite happened. **The transition to the market economy in China was decided with the goal of preserving and consolidating the power of the CCP.** This is no surprise, as Chinese communist leaders always asserted that objective. So far, this has been an unmitigated success! China's economy has been transformed in 40 years beyond recognition, and this has changed the world economy, and will influence the world's political arena in the twenty first century.

China's current system is one of **CCP power over a market economy.**³ Growth objectives were pursued using existing CCP institutions. CCP power has not faded with progress of market economy. On the contrary! Thanks to China's economic miracle of the last decades, the CCP has probably become the most powerful organization in all of world history.

The reinforcement of Communist State power has led to a state structure that is very different from that in Eastern Europe, even in the post-communist autocratic states that emerged from post-communist transition. This state structure is unique, and combines China's imperial state structure of the past and a very modern version of Leninism. The Communist Party stays very united and controls all the power levels. The Leninist principle of democratic centralism keeps the party united, as it forbids the formation of political fractions within the CCP. Fractionism is a major sin for Leninists. CCP members are officially allowed to express their opinion only in their own party unit. They are certainly not allowed to organize meetings outside the CCP's organizational structure. The CCP is present everywhere in Chinese society, not only inside the state apparatus, but also in private enterprises, sports clubs, schools and universities, apartment buildings, etc.. The CCP is very much present, albeit in a more secret form, in Hong Kong and Taiwan that it plans to take over in due time. The power of the CCP thus exceeds any governmental structure that we can think of, both in history and in modern times. Because the CCP exercises power by being everywhere in society, it is also in my view of a less expansionist nature, since it would be a very costly form of expansionism, requiring the CCP to span its fine grid network over a whole territory. China is already a continent. Communist leaders have openly stated that they want to take over Taiwan after Hong Kong, but for the

³ Because of the specificities of Chinese capitalism, some people tend to call it state capitalism (due to the still large role of the state sector) or crony capitalism (due to personal relationships between entrepreneurs and party cadres being used to give favors to the former, often in exchange for bribes). I do not object to those denominations. My emphasis is on the fact that China has become a truly capitalist economy, competing successfully on the global market. I would strongly dispute claims that China is *not* a market economy.

foreseeable future that is as far as their expansionism goes. There is for example no mention of taking over Mongolia or parts of Russia. I will dwell on this important point further below.

If the CCP has never been more powerful than it is now, why is there more and more censorship and restriction of freedoms under Xi Jinping? One may think that China's communist leaders are powerful enough that they could afford to somewhat relax censorship and repression. Autocracies, however, function very differently from democracies, and have their own logic. In a democracy, freedom of speech, and freedom in general, do not threaten elected leaders. They can be insulted, jeered and mocked, but this does not threaten their power, as they acquired it through legitimate contested elections. The mere fact that they were elected implies that they have a power base. Taking away freedoms from citizens would be a sure way to lose votes and political power. In an autocracy, leaders are not elected by universal suffrage, and they cannot count on such visible and official signs of public support as an election. Power inside an autocracy is usually lost to rivals inside the power structure. Autocratic leaders who are perceived as weak are more likely to be challenged by rivals. Therefore, they need to signal strength in order to deter potential challengers. An autocratic leader cannot thus leave any criticism of his rule unchallenged, even if that criticism does not directly represent a threat to his power. This is why absence of democratic selection of leaders under autocracy always goes hand in hand with repression, censorship and restriction of freedoms.

Having market economies under dictatorial regimes is nothing new. There have been dozens of dictatorial regimes in capitalist countries. What is historically new is that the Chinese system is one of a market economy under a communist dictatorship. This is indeed a paradox as the communist doctrine calls for the abolition of capitalism and its replacement with a socialist system. In China, the socialist system that existed under Mao Zedong has been replaced with a capitalist system. Communist ideology thus appears quite hollow given the Chinese experience. If anything, the historical experience has shown the superiority of the market economy over socialist central planning. The hollowness of the communist ideology, especially in the Chinese context, creates a challenge for Chinese leaders as that ideology appears to be non credible. The only reason it is used is as a signal of loyalty among cadres and leaders. Ambitious cadres who want to get promotion need to show good economic performance in the region under their supervision, but they also have to show that they can reproduce the slogans of the political campaigns organized by the Chinese leaders. The lack of a legitimate ideology to justify the power of the CCP is nevertheless a clear weakness. This means that CCP leaders must make more use of repression, terror and intimidation to stay in power. Once people are not afraid of the power of the CCP, the latter risks being overthrown. This will especially be the case if corruption that became widespread with the introduction of market reforms is not kept under control.⁴ Note, however, that even if communist ideology appears to be completely obsolete, the propaganda of the CCP can be very effective, especially since it is not challenged by any opposition parties that are not allowed to exist legally. As advanced western countries have shown weakness in recent years, especially since the 2008 crisis,

⁴ On that, see Roland (2018) or Li et al. (2017).

and with the continuous decline of American influence in the world, the CCP has been successfully making claims that China's existing communist regime works "better" than Western democracies. Interestingly, that propaganda is mostly for domestic consumption. Chinese leaders have not aggressively been making propaganda outside China, in contrast to Putin's trolls who have been extremely active in Western democracies, undermining elections and the institutions of the European Union. This brings us to try to understand the international strategy of the CCP leaders, given their choice of introducing the market economy to preserve and consolidate their power.

3. China's international strategy.

Given the miraculous growth China has experienced over the last 40 years, it has become impossible to ignore China's role in the world and in Asia. China will in the foreseeable future become the country with the largest GDP in the world, overtaking the US. China's population of nearly 1.4 billion people by far outstrips the population of any other country except India. In order to understand directions the international order is taking, one cannot ignore China. The difficulty in this endeavor is, as stated in the previous section, that China has a Communist regime and a thriving market economy, a combination that has never been observed so far.

The existence of democracies is obviously a challenge to CCP power, since democracies have a record of human rights and freedom that does not exist in China, but communist China also represents a challenge to the outside world. Many people fear that China's political regime may spread to other countries.

Other communist regimes collapsed because their socialist central planning system proved to be economically inferior to capitalism. Capitalism under CCP power continues to face a similar challenge. As long as catching up with the West takes place, CCP power should, in my view, be stable with very high probability. If China starts lagging behind the growth of the world economy, the CCP will face a big legitimacy problem. This is the foundation of the fear of low growth among Chinese leaders. Chinese integration in the world economy is necessary to maintain growth and prevent economic "falling behind". This may or may not succeed.

Recall that the main objective of Chinese leaders is to keep the Chinese Communist Party (CCP) in power. Deng Xiaoping thought that without major market reforms bringing growth, the CCP was doomed. He was right because this became indeed the fate of communist regimes in Eastern Europe. Maintaining the CCP in power is also the reason for China's rapid and successful integration in the world economy and for recent initiatives like the Belt and Road Initiative (BRI) that we will discuss below. China's leaders feel that if the Chinese economy does not grow as fast as the world economy, they will be blamed for it, possibly leading to an implosion of the Communist regime, like in Eastern Europe. Integration in the world economy therefore has this objective in mind. Access to world markets is thus crucial for Chinese leaders.

China, as a market economy, has become very dependent on the world economy for its growth. The legitimation of the regime is based on its high growth record relative to the rest of the world, but this growth record itself is based on export-led growth, as was the case with all Asian tigers. China's regime survival thus depends strongly on successful integration in the world economy. Without competition from the world economy, Chinese economic dynamism would likely fade away and the state sector might take again the dominant role in the economy.

In contrast to 20th century communism, China needs strong integration in the world economy. Differences in cultures and political regime with the rest of the world, and especially with advanced Western democracies, will nevertheless undoubtedly lead to frictions that must be managed peacefully. This is what we discuss in this section.

What are China's hegemonic objectives in the current world? It is very important to have an accurate answer to that question.

First of all, in terms of ambitions of territorial expansion, Chinese leaders have expressed the open goal of bringing Hong Kong and Taiwan into the mold of communist rule. It is happening in Hong Kong already. It is not clear how it will happen with Taiwan, but the Chinese leaders are patient. Apart from Hong Kong and Taiwan, China does not have ambitions of territorial expansion. It is important to repeat that a Communist regime has a higher cost of territorial expansion compared to other political regimes. This is because for Chinese Communists, as stated above, taking control of a territory implies the need to establish comprehensive CCP control over that territory, which takes time and is relatively costly. British colonialists for example never tried to have comprehensive control over their colonial territories.

It is also important to know that China is not interested in the spread of communist regimes worldwide, which was a clear objective of various Communist Internationals in the twentieth century and also an objective of Mao Zedong. As stated in the previous section, China is not doing any propaganda in favor of communism in foreign countries, in contrast to the Maoist years when it was very active in that domain. As explained above, this is because communist ideology is dead, following the failure of socialist economies. Inside China, communist ideology is only used formally, but mainly in order to justify existing policies, not at all as a future-oriented eschatology, as was done in the past by true believers of communism. Chinese leaders do not really believe in communist ideology, but they firmly believe in the goal of maintaining the CCP in power in China.

The absence of large territorial ambitions does not mean that China's growth will not lead to some forms of international instability. As it becomes more powerful economically and militarily, China will undoubtedly prove more aggressive in Asia, whether it is about borders in the South China Sea, territorial disputes with Japan, India, Vietnam and other neighboring countries.

If we believe current trends, China will also in the future be more aggressive in other domains: censorship beyond its borders (the Cambridge University Press episode being a good example), retaliation against what the Chinese leaders perceive as “anti-Chinese” actions. Lacking the soft power of democracies and not even trying hard to do propaganda for their own system outside China, Chinese leaders will resort more and more to threats and blackmail in order to silence criticism abroad of China’s denial of Human Rights to its citizens.

Because of their China-centered view of the world, Chinese leaders will not try to take leadership of the international order, but instead claim stronger influence in international organizations proportional to China’s economic and demographic power. Chinese leaders accept the existing multilateral international order because it brings more stability, which is to China’s advantage. Given its size and the importance of international integration for regime survival (China’s openness ratio is above 40%, whereas that of the US is below 30%), China cares a lot about the stability of the international order.

It would be, however, wrong to see China as one of the main defenders of the world order. China will tend to only pay lip service to international rules and is not likely to respect international decisions that go against its interest, but it is not the only country in that case. In the case of China, since CCP leaders view the right to self-determination as the highest principle in international relations, one should not expect them to invest too much in the international order or even try to shape the world in the direction of more multilateralism.

The long run coexistence of the Chinese communist regime and advanced democracies will be an important challenge in the future because of few shared values between these different regimes. Nevertheless, peaceful coexistence is in my view clearly possible, albeit with frictions, but it is also necessary. There is no realistic alternative. Therefore, peaceful coexistence with China should be an important goal for the international community.

The main challenge for the West is to better understand the nature of CCP power, understand its stability as well as its objectives. Mistakes can unnecessarily increase international tension. This would be the case for example if one thinks that CCP power can be overthrown through outside political pressure. Misreading China’s international economic initiatives for political expansionism would also be tragically misguided.

The Trump administration has expressed the misguided will to sabotage the “China 2025” program and the drive towards high tech innovation. This is pure bullying. While China’s moves to reduce the income and innovation gap with the West are

beneficial for the world economy, there is little chance that China will overtake the US in terms of fundamental innovation⁵.

Before the Trump administration, the Obama administration had made moves to try to isolate China from other Asian countries. The Trans-Pacific Partnership TPP could clearly be understood that way, The US government has always blocked moves to increase China's role in international organizations, be it China's representation inside the IMF or the refusal of the US government to participate in the Asian Infrastructure Investment Bank.

The biggest obstacle to coexistence with China is not so much related to trade, which has been beneficial to the whole world, but to foreign direct investment, in particular acquisition of foreign firms. On the Chinese side, there has been the fear that further economic opening will lead to loss of control of Chinese Communist Party over large sectors of the economy such as in banking, internet and social media. On the other side, there has been the fear that acquisitions of US firms by Chinese investors could be used for political control by the Chinese Communist Party. This argument is used to justify the view that one should block takeovers by Chinese firms. This fear is also widely shared in Europe, as was observed for example in Germany with the takeovers by Chinese firms of Kuka and Cotesa, that were heavily scrutinized before receiving the green light. This is likely to be a bone of contention for quite a while, independently of Trump's trade war against China. Even if relations between China and the rest of the world improve, it is unlikely that trust building will be sufficiently strong so as to remove concerns about the possibility of using takeovers as a form of political leverage. There are, however, many other ways China can invest outside its borders without raising the specter of the danger of political leverage. This is the case for greenfield investment and also for infrastructure investment. Both types of investment may increase China's influence, but do not contribute to diminish national sovereignty over existing firms, and therefore should raise less concern. As for infrastructure, once it is in place, it cannot be used for political blackmail, because it falls under the control of national governments wherever it is situated. Even when it comes to acquisitions, a country can use it for political leverage only if its control over foreign firms is sufficiently large. This means that, on both sides, there is clearly room for takeover activity as long as foreign control remains sufficiently limited. The Chinese leaders seem to have understood that they can tolerate more presence of foreign capital, for example in the banking sector, without feeling that their national sovereignty is threatened.

A major source of misunderstandings is due to the differences in political regime between democracy and communism. On the Chinese side, protests about human rights violation should not be interpreted as signs of US expansionism. In a democracy, the press is free and cannot be censored. Criticism of government is not perceived as weakness. Declarations by politicians on human rights violations serve

⁵ See in particular Roland (2018) on that point.

as signal to domestic voters. Chinese government pressure cannot make such declarations go away. They will always be there and should not be misinterpreted. Disapproval of the Chinese communist regime by the US does not mean that the US and China cannot coexist peacefully. The US has lost taste for international adventures and foreign “state-building”. The failure of the Iraq war showed then clearly the weakness of the US superpower whose decline has been accelerating with the Trump presidency.

4. Understanding the Belt and Road Initiative

In light of the two preceding sections, we can understand better the goals of the Belt and Road Initiative (BRI). As stated, its goal is to enhance China’s integration in the world economy so as to make sure China’s growth does not lag behind that of the world economy. How can one understand the main elements of the BRI in that context?

The BRI aims at financing infrastructure projects along the “silk road economic belt” linking China to Central Asia, South Asia and ultimately Europe. It also aims at securing a “maritime silk road” linking China to South East Asia, South Asia, Gulf countries, North Africa and Europe.

4.1. China’s motivations and interests in the BRI context.

It is important to understand first and foremost China’s economic and geopolitical interests in launching this initiative. As stated above, China’s further integration in the world economy is a key economic objective. As China’s growth rate will inevitably fall, as was the case with all Asian tigers, this will create a legitimacy problem for the CCP that delivered very high growth rates for 40 years since it started its market reforms. China’s best bet to continue delivering relatively high growth rates is to 1) have better access to natural resources, 2) to maintain high export growth. Also, as long as China’s growth rates are not below those of the world economy, CCP leaders can hope to minimize the risks of social disruption related to falling growth rates if these objectives are fulfilled. It appears that the BRI is designed precisely to fulfill those objectives.

First, China’s continued growth relies more and more on natural resource imports. Contrary to Russia for example, China depends heavily on natural resource imports. China is well endowed with a number of natural resources, such as rare earth for example, but it needs to import oil and gas, cobalt, lithium, copper, iron, gold and chrome. This is a direct consequence of China’s phenomenal growth rates. The BRI will directly help to facilitate imports to China by creating infrastructure to transport these imports. We explain this in a bit more detail below. Moreover, since infrastructure projects in BRI countries will be paid by debt, one way to repay debt is via exports to China. In that sense, BRI will help to stabilize imports to China.

Second, The BRI will also help increase Chinese exports. It will do so through various channels. First, the infrastructure investment will help reduce transport costs. Second, to

the extent that BRI investment improves trade relations with BRI countries, it will also help boost Chinese exports, both directly and indirectly. Closer international economic relations between China and other countries will generate business deals leading to direct increases in Chinese exports. Exports to China (the import motive for the Chinese) will be compensated to a certain extent by business deals to import Chinese products. Indirectly, to the extent that infrastructure investment helps the local economy, it will boost local growth rates, which should increase imports, and in particular imports from China. This effect is sure to be present to a certain extent because, from the local country's perspective, the BRI investment should lead automatically to an increase in exports to China, which should increase aggregate demand within the country, eventually leading to an increase in import demand.

Third, as a result of the last two points, the BRI will lead to increased imports to China, but also increased exports to the rest of the world, thereby anchoring China's growth in world economic growth, but also helping to boost the latter.

Without going into too much detail, the role of BRI in Central Asia is quite illustrative of China's motives. Central Asia has tremendous natural resources. Kazakhstan only, with a population of only 18 million, the largest landlocked country in the world, is endowed with a wide variety of large volumes of natural resources: oil, gas, coal, copper, iron, zinc, lead, gold, manganese, uranium, etc. When Kazakhstan was a Soviet republic, its natural resources were exported to the rest of the Soviet Union, mainly Russia, and it got little benefit from its natural resource endowment. Since its independence in 1991, Kazakhstan was able to diversify its exports and generate large revenues from natural resource exports. Russia is itself well-endowed with natural resources so economic complementarities between Kazakhstan and Russia are not that large, even though, for obvious political reasons, Kazakhstan has signed on to Russia's Eurasian Economic Union. On the other hand, there is a huge trade potential between China and Kazakhstan. The latter has relative abundance of natural resources and relative scarcity of labor. China has relative abundance of labor and relative scarcity of resources. China can thus benefit enormously from increasing natural resource imports from Kazakhstan, while the latter can gain from importing Chinese manufacturing goods. Transport costs have been an important impediment to growth of international trade between Kazakhstan and China. Roads and railway networks between the two countries have been insufficient, and BRI projects aim at substantially improving transport routes between the two countries. BRI projects should also help create better transport connections between Kazakhstan and Turkey, and Europe more generally. Kazakhstan would thus be at the center of much Eurasian trade transport. Given the numerous mountain ranges along the new silk road, infrastructure investment is key to create these Eurasian trade routes.

Note also that the new silk road route via Kazakhstan would have to cross Xinjiang province, the most Western Chinese province. It is probably no coincidence that the Chinese authorities have been cracking down in recent years not only on Islamic extremists but also on Ouigur separatists in sparsely populated -but geographically very large- Xinjiang province. They want to secure the BRI trade routes both internally and externally.

There is no doubt that BRI also benefits the world.⁶ Infrastructure investment that promotes trade is a win-win situation and should be welcomed as such. At the same time, one should not deny that there are geopolitical issues involved. At a time where the US under president Trump is engaging in a trade war with China and is taking initiatives to destroy the multilateral world order, it is no surprise that the BRI, that should have positive effects for globalization will be under attack from the Trump administration. The most sensitive aspect relates to the maritime silk road. Chinese leaders want to prevent military blockades that would close existential trade routes for China. The US has the capacity to block the Malaga strait, an important route for world maritime trade. The Chinese government aims thus to establish a number of naval bases to protect its maritime trade. A first base has been established in Djibouti, at the horn of Africa, a critical place for maritime traffic from the Mediterranean but also from the Gulf states. This will probably be seen as a military threat by the US that has many more naval and military bases around the world. It is nevertheless logical for China to deploy naval bases along the maritime silk road.⁷ The geopolitical tensions that may arise from China's economic and military deployment in Asia and along the Indian Ocean could prove to be very dangerous for world peace. Indeed, any Blockade of China's trade routes could lead to a military response from China. This had been the case before WWII when the embargo of exports of oil to Japan led the latter to invade the East Indies and to attack the US in Pearl Harbor. We hope the lessons from history will be learned and that peaceful international trade will be preserved.

4.2. Misgivings and problems with BRI.

The BRI is starting to generate more and more buzz in the media worldwide. Given the motives of Chinese leaders in setting up the BRI, it is important to get rid of misgivings about BRI while understanding its real weaknesses.

The most important misgiving is the fear that BRI is an instrument of Chinese leaders to take over the world. As explained above, the objectives of BRI are domestic in nature, and the Chinese political regime makes it very difficult and costly to take over a foreign territory. BRI is thus not intended as some neo-colonial initiative. A theme that has nevertheless come up repeatedly in the press in support of the "neo-colonial" interpretation of BRI is that developing countries that are having difficulties reimbursing BRI-related foreign debt will be "taken over" by China. The example that is usually given is the case of Sri Lanka. In the context of BRI, Sri Lanka borrowed money to build the Hambantota port and the Mattala International Airport. Both projects are examples of white elephants. Both have failed to generate traffic (the Mattala International Airport has only four flights scheduled weekly and the Hambantota airport has barely generated any cargo traffic). The Sri Lankan government has been unable to reimburse its debts related to those projects and thus sold both the port and the airport to China. What to make of it? It would be exaggerated to conclude that China is taking over control of Sri Lanka. If these are

⁶ See e.g. Garcia-Herrero and Xu (2017).

⁷ China's aggressive behavior in the South China sea is another issue. There are large reserves of oil below the sea floor and China wants to exploit them given its high need for fossil fuels

white elephant projects, they will not be of much use to China. In the best case, Chinese companies will be forced to use them, but it will not necessarily make them profitable. One cannot, however, exclude that they will be used as military bases. The contracts with Sri Lanka prohibit this, but that does not mean it may not happen. As explained above, China will need military bases to secure the safe transport of Chinese imports as well as exports. Whatever scenario one can think of, in no case does it mean that China is “taking over” Sri Lanka.

I would argue that the vulnerability related to excessive debt accumulated by BRI countries (Pakistan is also talked about, but it is not the only one) lies not with developing countries, but with China. Most BRI projects are infrastructure-related. Once they are built, the Chinese government cannot fundamentally take them away. Precisely for that reason, countries have an incentive to default on their debt once the BRI projects are built. They thus have an incentive to take up excessive debt that they will later default on. Of course, the Chinese government can take over the assets or part of them in case of a default, like in the case of Sri Lanka, but how do you take over ownership of a bridge, a road or a railroad? Governments can easily pass laws to de facto expropriate Chinese ownership over infrastructure. The Chinese government may find various ways of retaliating against governments who default on their debt, but it does not take away the fact that BRI infrastructure debts are forms of sovereign debt. We know from the sovereign debt literature that creditors over sovereign debt cannot use standard bankruptcy laws to recover their loans. We also know from that literature that, even if default has short term costs in terms of inability to borrow on the international market, this usually does not last long, and countries that default on sovereign debt are able to secure loans in the long run. The Chinese government may thus find itself in a position in the long run where a large proportion of BRI loans cannot be recovered, thus creating a financial problem for China. The optimal solution in case of sovereign default is to agree on debt renegotiation. The Chinese government may, however, face substantial haircuts as a consequence of such renegotiations.

Whatever the outcome, infrastructure investments in developing countries that make economic sense and are not white elephants are beneficial to the world economy. It is precisely for the latter reason that it would be wrong to refuse to participate in BRI initiatives. The recent deal with Italy to revive the port of Trieste (near Venice on the Adriatic sea) should benefit badly needed job creation in Italy and revive the region around Trieste.

While it is important to debunk wrong interpretations of BRI, one should also grasp the major weaknesses of the Chinese initiative.

First, it exemplifies the phenomenon of rent-seeking by Chinese firms, which is generally ignored by observers of the Chinese economy. Many Chinese firms have been eager to join the BRI bandwagon because of opportunities to produce and export new goods. This is probably one of the reasons, though certainly not the only one, Many BRI projects are really white elephants. Chinese firms involved do not suffer the consequences of participating in inefficient projects as long as they get paid and can boast about generating foreign export

revenues. By design, BRI projects should be built by Chinese firms. This has led to various forms of rent-seeking behavior by Chinese firms to be “included” in BRI projects even though these projects are either inefficient or not really related to infrastructure-building.⁸ This rent-seeking is in essence similar to the process leading to the selection of investment projects within China.

Second, a related phenomenon is that the expansion of BRI, and of Chinese international presence in general, has brought forth an expansion of corruption. Officials in developing countries have been showered with bribes in order to accept BRI projects. This has led to cost inflation making the projects more expensive to pay for, while kickbacks to local politicians have secured their approval. This corruption not only paves the way for inefficiencies and diversion of funds in the implementation of BRI projects, but also creates political links between China and local politicians. Chinese officials have no second thoughts in bribing officials and politicians in developing countries, even though such corruption is strongly punished at home. There is an element of “Chinese exceptionalism” at play here that is related to a strong Chinese-centric attitude in international affairs. To the extent that corruption of foreign dignitaries is in the interests of China, then it is seen as somewhat morally right. The fact that norms are different inside China is irrelevant here. It is only if corruption scandals abroad damage Chinese interests that Chinese leaders may decide to change their policy. I hesitate in making comparisons and parallels with “American exceptionalism” though there are certainly differences.

Third, China has no experience in dealing with sovereign debt issues, and is likely to make mistakes as countries start defaulting on BRI-related debts. A too tough attitude risks China being perceived as a neo-colonialist power infringing on national sovereignty of other countries. A too lax attitude risks China being perceived as weak and encouraging more loan defaults. The former seems more dangerous for world peace as it could lead to military conflicts that could internationalize very fast.

Fourth, and this is also directly related, China is becoming too strong too fast. Its economic power is becoming on par with that of the US. China’s foreign policy experts are by far not as competent as the economic experts who have guided economic reforms in the last 40 years. China is very likely to make mistakes in handling any foreign tension related to BRI. Chinese leaders have shown great patience and control in dealing with Trump’s trade war. At the same time, the US bullying attitude in the whole process is generating a lot of pent-up frustration. Chinese leaders will be tempted to show strength in a more minor issue, thereby leading to risks of escalation that could degenerate easily.

Despite these caveats and clear weaknesses, BRI is not bad for the world. It is not fruitful to try to oppose it or to try to sabotage China’s increasing role in the world economy. The international community gains in cooperating with China in its BRI initiative. China’s global expansion is inevitable. One cannot oppose it, one can only learn how to live with it. On the other hand, China has recently been presented as more threatening than it really is. As we

⁸ For a good description, see Yu (2018).

hop to have demonstrated, it will have enough on its arms in dealing with the inherent weaknesses of th BRI project itself.

5. Conclusion.

There has been a lot of confusion in understanding the motives behind China's BRI initiative. We have argued that it is best understood in terms of the long term strategy of Chinese communist leaders to hang on to power. That was the motivation behind market reforms that spurred 40 years of very high growth. Given the importance that China has gained in the world economy, and its need for natural resources and export markets to continue to sustain its growth, BRI is the answer the Chinese leaders came up with. It is a survival strategy of Chinese leaders, but it will deeply affect the future of world trade, and possibly of world peace.

REFERENCES

- Bardhan, P. (2012) *Awakening Giants, Feet of Clay: Assessing the Economic Rise of China and India*, Princeton University Press, Princeton N.J.
- Dewatripont., M and G. Roland, 1995, "The Design of Reform Packages under Uncertainty" *American Economic Review* 85(5) : 1207-1223.
- Garcia-Herrero and J. Xu (2017) "Chinas Belt and Road Initiative: Can Europe Expect Trade Gains" *China and World Economy* 25(6): 84-99.
- Li, W., G. Roland and Y. Xie (2017) "Crony Capitalism, the Party State and Political Boundaries of Corruption", Working Paper UC Berkeley.
- Roland, G. (2018) "Coexisting with China in the twenty first century" *Acta Oeconomica* 69(1): 49-70.
- Xie, Y. and Y. Xie, (2017) "Machiavellian Experimentation" *Journal of Comparative Economics*, 45(4): 685-694.
- Xu, C. (2011) "The Fundamental Institutions of China's Reforms and Development", *Journal of Economic Literature* 49(4): 1076-1151.
- Yu, J. (2018) "The Belt and Road Initiative: Domestic Interests, Bureaucratic Politics and the EU-China relations" *Asia-Europe Journal* , 16(3): 223-236.