The Strategy of Influence behind China's Belt and Road Initiative

Ioana Petculescu*

DAVA *Analytic Brief* No. 7, April 2018

This Analytic Brief is the second in our series regarding Strategic Doctrines in the Asia-Pacific. For previous documents see the dedicated section.

Introduction

China has systematically presented its Belt and Road – or One Belt, One Road – Initiative (BRI) as an international development project, destined to build a "community with a shared future for mankind" throughout Eurasia and beyond. In official discussions and statements, Beijing has carefully avoided the word "strategy," which might have created the impression that the generous offer of massive investments in infrastructure along the new Silk Road conceals in reality an imperial and hegemonic design. Nonetheless, suspicions as to the real motifs of the BRI persist, especially in light of the Chinese military buildup and reforms undertaken in recent years.

This military rejuvenation of the nation launched by President Xi Jinping since 2013, coupled with controversial territorial claims in the South China Sea and with the promotion of an alternative model to the Western order, has some in Europe wonder whether China's offer of cooperation is sincere. Iva and Zelimir Zivkovic have rightly observed in a previous DAVA Mercantile Digest that "China is a State and a rising global power, not a corporation or (even less) a charity foundation. As has been shown by the recent votes by Portugal and Greece concerning the E.U. position on China and investment screening procedures, crucial economic support in times of need can translate into remarkable political clout." This is precisely the reason why the Chinese presence in Europe is more and more perceived not just as an opportunity, but also as a threat, including to national security.

In the current era of fast technological change and growing importance of innovation, Chinese investments have become a specific concern for many European officials, who worry about the integrity and competitiveness of the local industrial base, especially in strategic sectors. To address these concerns, the European Union and the governments of certain Members States have envisaged the imposition of restrictions on foreign direct investments (FDI), often focusing on areas such as artificial intelligence, cyber and other sensitive technologies. In particular, the Commission has proposed last year a new regulation for the control of FDI in the E.U. Although a welcome development, the uniform implementation and the ultimate effectiveness of such measures look anything but certain. Yet, they are absolutely necessary if Europe wishes to protect its critical economic assets and rebalance the asymmetric relationship with China in terms of FDI inflow.

Land Belts and Sea Roads for Power Projection

For many years, the *dictum* of the Chinese foreign policy has been that of "peaceful development" or, according to some other iterations of the same formula, of "peaceful rise." Expressing the vision of a great power with global ambitions, the BRI is obviously part of this "peaceful rise" and the guarantee of China's continued economic growth. At the same time, the two components of the BRI, namely the Silk Road Economic Belt and the 21st Century Maritime Silk Road, should also allow China to project itself more easily beyond its borders and rise not just economically, but politically and, one would say, militarily.

The routes and roads that Beijing plans to build with the now 71 countries having joined the BRI would foster the emergence of a network connecting China with hubs in Central Asia, the Middle East, Africa and Europe. These hubs are as important for economic development as they are essential for achieving geostrategic goals. Take the new Maritime Silk Road. Its similitude to what the experts have called the "String of Pearls" military strategy is striking and has prompted some of them to conclude that this is just a terminological distinction without a difference. In both cases, the end result is access to ports located near maritime choke points in the Indo-Pacific for the People's Liberation Army's Navy (PLAN). And as noted by one analyst, the blurred distinction between Chinese civilian and military vessels, such as those operating in the South China Sea, further smudges the line between a military-based "String of Pearls" and a trade-based "Maritime Silk Road."

The China-Pakistan Economic Corridor (CPEC) is one example illustrating the close connection between the economic and the military aspects of China's foreign investment policy. Through CPEC, China has been financing four railways, three roads and one canal projects, which should contribute to the belt around China's Heartland. At the same time, the road to China's growing maritime influence in the Indo-Pacific goes via the port of Gwadar in Southern Pakistan.

Gwadar, which is located near the Strait of Hormuz, is definitely one of the "pearls" of the "string" methodically created by Beijing in the region. Access to that port via roads, railways and, according to the current plans, pipelines shows the BRI's indisputable strategic benefit to China. On the one hand, it offers China the possibility to escape the "Malacca Dilemma" and, as observed by CFR's Ely Ratner, the "vulnerabilities that result from having to ship much-needed energy imports through the South China Sea and up the east coast of China, where U.S. and other regional militaries have the capabilities to threaten or block maritime traffic."

On the other hand, this access is likely to be exploited by PLAN to enhance its presence in the Indian Ocean and deploy force projection capabilities. China has invested in the development of a deep-water port there, which means that Gwadar might be able to host a blue-water navy, such as the Liaoning carrier group. While Beijing has been obviously careful not to associate this development project with any military purpose, analysts agree that China could at least use port facilities in the Indian Ocean on a commercial basis for specific purposes and contingencies, for example, for the positioning of Chinese "civilian" service providers or of spare parts and munitions.

China is well aware of geopolitical theories, such as those developed by the American naval strategist Alfred Thayer Mahan and linking the dominance of the seas to economic prosperity and great power status. Accordingly, Beijing has undertaken to establish a vast network of naval facilities in South Asia, which includes, in addition to Gwadar, the ports of Chittagong in Bangladesh, Hambantota in Sri Lanka, Marao in the Maldives and Kyaukpyu in Myanmar.

In the future, ports in the Mediterranean will join this network of Chinese-developed maritime installations in the Indo-Pacific. Thus, Venice will be the Maritime Silk Road's final destination in Europe. To take advantage of the BRI's investment potential, Venice has already formed with the Italian port cities of Ravenna and Trieste and with those of Koper (Slovenia) and Rijeka (Croatia) the North Adriatic Port Association (NAPA). Due to such initiatives, China's influence is likely to expand far away from its shores. The maritime road, therefore, contributes decisively to making the Chinese Dream of "national rejuvenation" a reality.

Xi's Dream of Chinese Military Rejuvenation and Innovation Leadership

President Xi's "dream of national rejuvenation" also has a military component. China's return on the world stage as a great power is impossible without modern armed forces, able to compete with the forces of the other great powers. This is also a question of national pride. The Chinese have a vivid memory of the country's humiliation by the "Western imperialists" during the Opium Wars of the 19th century. Accordingly, the Chinese leadership "has made modernization an explicit goal, citing the need to catch up with the West," including with regard to weaponry.

Military modernization has impacted policy and the force alike. In 2015, Beijing launched the most significant reform program in thirty years, aimed at enabling the PLA "to wage modern warfare by updating the military's structure, its command and control, and, in particular, its service branches' ability to conduct joint operations" in contested environments. Importantly, the same year China released its latest Defense White Paper (DWP), a fundamental document describing the country's military posture. According to the DWP, "China's national strategic goal is to complete the building of a moderately prosperous society in all respects by 2021 when the [Chinese Communist Party (CCP)] celebrates its centenary; and the building of a modern socialist country that is prosperous, strong, democratic, culturally advanced and harmonious by 2049 when the People's Republic of China (PRC) marks its centenary." Taking advantage of what it considers to be a "period of strategic opportunity," the Chinese leadership has set out ambitious tasks for its armed forces, while emphasizing that the PLA's primary mission remains to "uphold the leadership of the CPC and the socialist system with Chinese characteristics." As to the connection between economic growth and military strength, the DWP indicates that "[b]uilding a strong national defense and powerful armed forces is a strategic task of China's modernization drive and a security guarantee for China's peaceful development."

In practice, since 2015 the Chinese government has stepped up investments in new equipment and military capabilities. China may afford such investments due to a steady increase in defense budgets. According to SIPRI, China increased its military spending by 5.4% to $215 billion, a much lower rate of growth than in previous years, but still quite impressive. The real level of Chinese defense spending is, anyway, a subject of controversy. What is certain, however, is that China is today the second largest military spender in the world after the United States and, subject to sustained economic growth, will likely keep up defense spending in the years to come.

China has used this money to develop sophisticated guns, aircraft, missile systems and, of course, ships. Indeed, China has spent considerable amounts on the modernization of its maritime assets. In addition to the JIN-class ballistic missile submarines and sea-launched ballistic missiles, ensuring a secure second strike capability for strategic deterrence, PLAN possesses the largest number of vessels in Asia, including multi-mission ships equipped with advanced anti-ship, anti-air and anti-submarine weapons and sensors.

Of note, in April 2017, China launched its second aircraft carrier and the first entirely built on its own. The new carrier is based on PLAN's sole operational aircraft carrier to date, the Liaoning, which is a Soviet-era Kuznetsov-class carrier Varyag acquired by China in 2012. The carrier program is a critical part of China's maritime expansion. Defense News recently reported that this program has accelerated and pointed at a press release of the state-owned China Shipbuilding Industry Corporation, or CSIC, which mentioned the shipbuilding group's broader efforts "to achieve technological breakthroughs in nuclear-powered aircraft carriers, new nuclear-powered submarines, quieter conventionally powered submarines, underwater artificial intelligence-based combat systems and integrated networked communications systems."

Still, all these technological breakthroughs require substantial investments in research and advanced engineering. As a result, the Chinese leadership has unsurprisingly embraced innovation as one of its priorities and Xi Jinping has included it in his political thought, now part of the Chinese constitution. In his speech at the opening of CCP's 19th National Congress last October, Xi described innovation as "the primary driving force behind development" and "the strategic underpinning for building a modernized economy." At the same time, the Chinese President made an unambiguous statement as to the role of innovation for building a modernized military: "We must keep it firm in our minds that technology is the core combat capability, encourage innovations in major technologies, and conduct innovations independently."

His stated ambition is to make China the global leader in innovation by the middle of the century, when the country should also reach the status of the most powerful military force on the planet. To achieve these goals, Beijing already uses a variety of means, including the acquisition of stakes in foreign companies at the forefront of the current technological revolution. DAVA's expert Nani Klepo usefully exemplifies this aspect with her reference to the investment made by the Chinese Camel Group in the Croatian electric cars manufacturer Mate Rimac. Such tactics, in turn, raise concerns in the host countries, where governments now begin to realize that Chinese investments represent in reality a double-edged sword.

The Hidden Face of Chinese Investments and Europe's Belated Response

Several studies by research institutes and reports by media outlets have noted lately a significant boost in foreign takeovers of European companies, notably through state-owned enterprises (SOE). Their attention has obviously concentrated on Chinese investments due to the preponderance of SOEs and the characteristics of their transactions in the E.U. For example, a study commissioned by the Danish Business Authority and released earlier this year has observed that mergers & acquisitions (M&As) "by Chinese investors differ from the investment pattern of all third country investors. *First*, Chinese investors more often than other investors conduct M&As in Germany and the Netherlands. *Second*, Chinese investors also invest differently across sectors than other third country investors with a high concentration of M&As in the manufacturing sector."

Furthermore, according to another report published by Bloomberg, during the past two years Chinese investments in Germany have remarkably "shifted toward high-tech companies," a trend that has understandably "caused deep unease that Europe might lose control of important technological innovations and methods." Finally, a European Parliamentary Research Service briefing has warned that in 2016 "the flow of Chinese foreign direct investment (FDI) into the EU hit record levels, in sharp contrast to the continued decline in EU FDI flows to China" and that Chinese FDI have targeted "cutting-edge technologies in particular."

This comes as no surprise. In the words of DAVA's senior expert and co-founder Horia Ciurtin, "China … must ensure … that it can first benefit from European know-how in order to increase its own innovative capacity." This means that Europe must carefully assess any transfer of know-how to Chinese companies, especially when such transfers could affect key technologies concerning the national and economic security of the Union and of its Member States and, most probably, the future of warfare.

And this is what the EU intends to do from now on, by putting in place a screening mechanism for foreign direct investments. Similar mechanisms already exist in 12 Member States, where governments review FDI in strategic sectors on national security grounds. In order to stop what it calls "technological looting," France, for example, has strengthened its regulations by extending the authorities' scrutiny of acquisitions of French companies by foreign entities to new sectors, including digital data and artificial intelligence.

Building upon such national measures, the European Commission has advanced a Proposal for a Regulation establishing a framework for screening foreign direct investments in the European Union. In addition, the Commission envisages establishing a cooperation mechanism to harmonize the practices of the various Member States. Most importantly, it seeks to protect projects and programs of Union interest against non-transparent investments, in particular in the areas of research (Horizon 2020), space (Galileo), transport (Trans-European Networks for Transport, TEN-T), energy (TEN-E) and telecommunications.

The Commission is also bound to carry out by the end of the year an in-depth analysis of FDI flows into the Union, "focusing on strategic sectors (such as energy, space, transport) and assets (key technologies, critical infrastructure, sensitive data) whose control may raise concerns for security, or public order reasons. This is particularly the case when the investor is owned or controlled by a third country or benefits from significant state subsidies." To justify this new approach to FDI, the Commission explains that while E.U.'s openness to foreign investments remains the rule, "it has to be accompanied by vigorous and effective policies to, on the one hand, open up other economies and ensure that everyone plays by the same rules, and, on the other hand, to protect critical European assets against investment that would be detrimental to legitimate interests of the Union or its Member States."

The Commission's task will, however, not be easy. With time already running out, the adoption of the proposed regulation will take years, not months to be completed, since it supposes following the complex decision-making process under the ordinary legislative procedure set out in Articles 289 and 294 of the Treaty on the Functioning of the European Union. Moreover, this procedure involves not just the Commission and the European Parliament, but also Member States represented in the Council, who are likely to have the ultimate word on the matter.

Unfortunately, Europe is split between those at the center, who worry about the potentially nefarious purposes behind Chinese investments, and those at the periphery, who crave for foreign funds to support their weakened economies after the debt crisis. As indicated above, a group of opponents to the screening mechanism has emerged, consisting essentially of states from southern Europe, notably Greece and Portugal. Finally, foreign investment screening mechanisms have their own drawbacks and may prove to be at best ineffective and at worst counterproductive. Like any restrictive measure, the proposed regulation may be perceived, especially in the current climate of confrontation on trade issues, as a protectionist move, thereby exercising a deterrent effect on direct investments.

In addition, it may compromise the conclusion of the free trade agreements (FTAs) currently under negotiation between the E.U. and third countries, including China. Last but not least, the Union and its Member States should pay attention to any legal consequences that may stem from restrictions on foreign investments under these agreements, which also include investment promotion and protection clauses.

In this respect, Nikos Lavranos, an expert in international investment law and arbitration, has correctly observed that "the application of such a screening mechanism could lead to discriminatory treatment of foreign investors and hence to investment arbitration cases as result of breaches of the FTA provisions."

The challenges to the Commission's proposal are, therefore, numerous. Europe must, nevertheless, confront them. "*Timeo Danaos et dona ferentes*" goes the old saying about Greek gifts. Today, one should beware of China bearing gifts. Without discarding the benefits of the participation to the BRI, the institutions of the European Union and the governments of its Member States must primarily ensure a level-playing field for European companies in an increasingly competitive economic and geostrategic environment. Europe should bear in mind the thoughtful words of Graham Allison: "the Chinese view holds that China's rightful place is atop the pyramid; other states should be arranged as subordinated tributaries." The EU should never accept a subordinated role, but rather work to develop a partnership among equals with Beijing.

Ioana Petculescu, guest expert of DAVA | Strategic Analysis, is a lawyer specialized in international arbitration and litigation, practicing in Paris. She acts as a consultant for the aerospace and defense industry and as an expert for the European Union. She received a PhD in public international law from the University of Strasbourg, where she started her career as a lecturer. In addition to law, she also studied international relations, conflict analysis and geopolitics at the Catholic University of Louvain.